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Vol. I

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Sup. Ct.

TRANSCRIPT OF RECORD

(Pages 1 to 368)

Supreme Court of the United States

OCTOBER TERM, 1945

No. 278

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.

No. 279

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vs.

GUY A. THOMPSON, TRUSTEE, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

PETITION FOR CERTIORARI FILED JULY 30, 1945.

CERTIORARI GRANTED OCTOBER 8, 1945.

SUPREME COURT OF THE UNITED STATES

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INTERSTATE COMMERCE COMMISSION

Denver & Rio Grande Western Railroad Company Reorganization

SUBMISSION OF PLAN OF REORGANIZATION PURSUANT TO SECTION 77 OF THE BANKRUPTCY ACT, AS AMENDED

FINANCE DOCKET NO. 11002

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WASHINGTON, D. C.
APRIL, 1944

EXHIBIT A

INTERSTATE COMMERCE COMMISSION

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY
REORGANIZATION

Distribution of new securities per $1,000 principal amount of present bonds with accrued interest to January 1, 1943.

Outstanding Issue	Principal Amount Outstanding	Class of Present Security Designated in Court's Order of Classification	First Mortgage Bonds	Income Bonds	Preferred Stock	Common Stock
Denver & Rio Grande Consolidated 4's	$34,125,000	6	$318.92	$217.08	$321.60	$482.40
Denver & Rio Grande Consolidated 4½'s	6,382,000	6	329.03	223.97	331.80	497.70
Rio Grande Western First Trusts	15,190,000	7	970.20	349.80		
Rio Grande Western Consolidated's	15,080,000	8		266.00	970.90	93.10
Refunding and Improvement (Series A) 6's	2,000,000	10(a)	264.61	168.94	328.90	732.55
Refunding and Improvement (Series "B") 5's	12,000,000	10(b)	250.01	159.61	310.75	692.13
General 5's	29,808,009	11				146.10

Note: The treatment accorded the Reconstruction Finance Corporation and the Denver & Salt Lake bondholders and stockholders in case the consolidation provided for in the plan is or is not effected, is shown in Appendixes A and B on pages 182 and 183 hereof.

PLAN OF REORGANIZATION OF THE DENVER & RIO GRANDE WESTERN RAILROAD COMPANY, APPROVED BY THE COMMISSION IN ITS SUPPLEMENTAL ORDER OF JUNE 14, 1943, AND BY THE COURT, IN ITS ORDER OF OCTOBER 25, 1943.

Further investigation of the matters and things involved in this proceeding having been made upon petitions filed, and this Commission having, on the date hereof, made and filed a supplemental report containing its findings of fact and conclusions theron, and a full statement of the reasons for its conclusions, which report is hereby referred to and made a part hereof:

It is ordered, That the second supplemental report and order of July 13, 1942, approving a modified plan of reorganization of The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor, be, and it is hereby, further modified to read as follows, and as so further modified, is hereby approved:

Effective date.—A. The effective date of the plan shall be January 1, 1943.

The effective date of the plan shall determine the extent to which the claims of present creditors shall be capitalized in new securities, but the plan shall not affect creditors' claims until the new securities are actually issued by the reorganized company under the plan, and the carrying out of the plan shall not require any retroactive change in the operations of the debtor's trustees, or in their accounts, or in the reports made to this Commission or in any other reports or returns for the period prior to the date when such new securities are issued. Subject to the approval of the court, the reorganization committee may cause any issue of new securities to be dated as of a date other than the effective date (January 1, 1943), but only if the creditors who receive such issue of new securities shall receive the same treatment in respect of accruals of interest as if such issue of new securities had been dated January 1, 1943.

Reorganized company; consolidation.—B. The properties of the debtor, the secondary debtor, The Denver and Salt Lake Railway Company, hereinafter called the Salt Lake, The Rio Grande Junction Railway Company, hereinafter called the Junction, and the Goshen Valley Railroad Company, hereinafter called the Goshen Valley, shall, except as hereinafter otherwise provided, be merged or consolidated, to the extent legally possible, by transfer of the

subsidiary properties and the property held by the trustees, to the reorganized debtor or by transfer of all the properties to a new corporation organized for the purpose, hereinafter referred to as the new company, as may be determined by the reorganization committee. Consolidation of the Salt Lake with the debtor's properties shall be effective if, and only if, the holders of at least 90 percent in aggregate principal amount of Salt Lake income bonds voluntarily consent, within 90 days of the submission of the proposal to them to the modification of their rights, for which provision is hereinafter made. Unless such consents are obtained from the holders of the Salt Lake income bonds within the period stated, no actual consolidation of the Salt Lake and the Salt Lake Western with the debtor will be effective, and in that event only the properties of the debtor, the Junction, and the Goshen Valley shall be merged or consolidated in the manner indicated above; no provision will be made for the Salt Lake stock held by the public, and the trackage agreement will remain in effect. The merger or consolidation of the properties, including the Salt Lake, if the proposal is accepted by the holders of the required percent of bonds, shall be effected in a manner to be determined by the reorganization committee, subject to approval by this Commission and the court, and under a fair and equitable arrangement to protect the interests of the railroad employees affected, as required by law.

In the event that it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan in its application to the other interests, the judge may order consummation of the provisions of the plan other than those applicable to the distribution of securities to the Junction bondholders, and the Junction consolidation. Under these circumstances the Junction stock and the Junction lease should become assets of the reorganized company, subject to the liens of the mortgages of the reorganized company with provision for their release in the event of consolidation of the Junction with the reorganized company, and the Junction lease, in the discretion of the reorganization managers of the reorganized company and the judge, may be disaffirmed.

The new company shall be deemed to have come into possession of the properties as of the effective date of the plan.

New capitalization.—C. The capitalization of the new company, as of January 1, 1943, after consummation of the plan including the merger or consolidation of the Salt Lake, shall consist substantially of the following securities, excluding those to be pledged, the amounts stated being subject to reduction to the extent, if any, that matured interest proposed to be funded in the plan is paid, and

as equipment obligations or other liabilities are paid or reduced, and subject to variation as may be necessary, if so determined by the reorganization committee, to avoid the issue of scrip in denominations not expressible in even dollars or even hundredths of a share: Equipment-trust obligations, $5,758,000; new first-mortgage series A bonds, $38,573,680; new income-mortgage 4½-percent bonds, $29,750,184; bonds of the Denver & Salt Lake Railway Company, $11,234,000; a secured note or notes to the Chase National Bank, in the approximate amount of $2,158,458 (subject to a final determination of the amount of interest due on the present note, as of January 1, 1943); $32,531,220, par value, of new 5-percent preferred stock; and $35,167,585, par value, of new common stock.

In the event that the merger or consolidation of the Salt Lake is not effected, the capitalization of the reorganized debtor, as of January 1, 1943, excluding securities to be pledged, the amount stated being subject to reduction or variation, as provided above, shall consist substantially of $5,758,000 of equipment obligations, $33,373,680 of first-mortgage bonds, $21,049,579 of income bonds, a secured note or notes to the Chase National Bank in the approximate amount of $2,158,458, subject to the condition for such note stated above, the claim of the Finance Corporation, provided for in the manner hereinafter described, $32,120,120, par value, of 5-percent preferred stock, and $35,167,585, par value, of common stock.

Upon the consummation of the plan, including the consolidations, and the issue, distribution, and modification of securities as herein provided, the existing stocks of the debtor and its affiliated companies, together with all mortgage bonds issued and outstanding, including bonds pledged, and excluding all bonds of the Salt Lake, shall be surrendered to the reorganization committee and canceled, and all mortgages, other than the Salt Lake, shall be satisfied of record and canceled. In the event that consolidation of the Salt Lake is not effected, the stocks to be surrendered and canceled shall not include those of the secondary debtor and the Salt Lake.

Both the debtor and the secondary debtor shall be included within the plan.

The new company shall assume obligation in respect of all outstanding equipment obligations of the debtor and of the debtor's trustees. The interests of the holders of such claims are found not to be materially and adversely affected by the plan.

New first-mortgage bonds.—D. The new first mortgage shall constitute a first lien, subject only to the lien of equipment-trust obligations, on (1) all property owned by the debtor, the secondary debtor (in the event that consolidation with the Salt Lake is

effected, otherwise excluding the secondary debtor), or their trustees in bankruptcy as such, the Junction, and the Goshen Valley, at the time of effectuation of the plan, including securities, equipment, and the equity in such equipment as may be subject to equipment-trust obligations, but excluding the narrow-gage railway lines of the debtor, and equipment and property essential to the operation thereof, and excluding also the capital stock of the Utah Fuel Company; and (2) all property acquired by the new company after the date of the new first mortgage for use on or in connection with the mortgaged property subject only to such encumbrances or purchase-money liens as may exist or be created at the time of acquisition. So far as the reorganization committee, hereinafter provided for, may deem practicable, such lien shall be in the form of a direct mortgage, but it may take the form of the pledge or assignment of securities of a corporation or corporations owning property to which the lien is intended to extend. In the event of the consolidation of the properties of the Salt Lake as a part of the new system, the new first mortgage shall constitute a lien on such properties subject to the lien of the Salt Lake first-mortgage bonds and income bonds, so long as any of such bonds remain outstanding.

The first mortgage shall contain an appropriate provision in such terms as the reorganization committee shall determine, that the trustees under the mortgage may at any time release from the lien of the mortgage any of the mortgage property no longer required in the operation of the railroad, the proceeds from any sale or other disposition thereof to be equally and to the same extent held subject to the lien of the mortgage, as was the property so sold or disposed of. These provisions shall in no event operate to prevent the issue of equipment obligations with liens on equipment superior to the mortgage lien.

The first mortgage shall contain a covenant that the new company will at all times keep the mortgaged property supplied with such amount of motive power, rolling stock, and equipment (upon which the new first mortgage shall constitute a paramount lien subject only to such purchase-money liens as may be permitted by the terms thereof), and maintain the same in such condition as may be necessary for the efficient and economical operation of the mortgaged property.

The first-mortgage bonds may be issued in series, all equally secured as to principal and interest. Approximately $38,573,680 of series A bonds shall be issued in connection with the reorganization in partial settlement of claims, and additional series A bonds as may be necessary for the purpose of pledge, as provided in the plan. The series A bonds shall have a term of 50 years and shall

bear fixed interest at the rate of 3 percent per annum, and, in addition, fully cumulative prior contingent interest at the rate of 1 percent per annum, but subject to the right of the bondholders to postpone any interest payments, as hereinafter provided. Fixed interest shall be payable semiannually and prior contingent interest annually. Installments of interest on the new first-mortgage bonds becoming due before the plan is consummated shall be payable upon consummation of the plan.

The series A bonds shall be redeemable, in whole or in part, at a premium, initially not to exceed 5 percent, the rate thereof to be reduced during the life of the bonds according to a prescribed scale. Subject to such condition, the redemption provision shall be on such terms as the reorganization committee may determine.

Additional bonds, other than series A, shall be issuable under the mortgage without limit, or within such limit as may be specified in the mortgage, having such dates, maturities, coupon rates, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission. Such additional bonds shall be issuable on such bases, including the refunding of debt and the deposit of cash as shall be prescribed in the mortgage, provided that (1) bonds may be issued on the basis of additional property, including new equipment free from any other lien, and additions and betterments only to the extent of 75 percent, less prior lien debt, of the net amount of such additional property or additions and betterments, computed on the basis of cost, including prior lien debt, thereof or value thereof to the new company, whichever may be less; and (2), if consolidation with The Denver and Salt Lake Railway Company is effected in accordance with this plan, and when on any interest payment date for first-mortgage bonds the aggregate principal amount of new first-mortgage bonds outstanding, together with Denver and Salt Lake Railway Company first-mortgage bonds and income bonds, plus all other funded debt bearing fixed interest, shall exceed either 45 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest, other than bonds issued under the first mortgage, from 65 percent of the total capitalization at the time outstanding, the new company shall pay to the trustee of the new first mortgage, as a sinking fund, a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, prior contingent interest charges, the payment to the capital fund, contingent interest, and sinking-fund payments, as hereinafter prescribed; but, in the event such consolidation with The Denver and Salt Lake Railway Company is not

effected, the foregoing requirement of 45 percent for total fixed interest bearing debt shall be 40 percent. Such sinking fund shall be applied to the retirement of first-mortgage bonds by purchase in the open market or by call for tenders at not exceeding the redemption price (or in the case of bonds not redeemable, the principal amount and accrued interest), and, whenever the amount in the sinking fund exceeds $50,000 and first-mortgage bonds are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the sinking fund shall be applied to the redemption of new first-mortgage bonds on the next succeeding interest payment date. All bonds so acquired shall be canceled, and no bonds may be issued to refund any such bonds. First-mortgage bonds and income mortgage bonds outstanding shall be deemed to include all bonds authenticated and delivered to the new company which shall not have been canceled or assured of retirement through the deposit of cash. Funded debt shall include an amount equal to the capitalized value at 5 percent per annum of fixed rents payable for leased roads, other than terminal properties, but shall not include *(a)* obligations, other than mortgage bonds or equipment trust obligations, maturing not more than 2 years after their date, or *(b)* obligations of longer maturity secured by pledge of bonds having a lien on property of the reorganized company except to the extent, if any, by which the principal amount of such obligations exceeds the principal amount of such bonds so pledged. Bonds which may be guaranteed by the new company as to interest or principal or both, other than bonds of a terminal company, shall be included in funded debt, but, in case of a joint or several guaranty with other corporations, only to the extent of the new company's basic proportion of the principal liability. There shall be included in determining total capitalization only *(a)* obligations constituting funded debt, *(b)* stock having par value, at such par value, and *(c)* stock without par value, at $100 a share, and, in case of other stock, at the capital value at which such stock is carried on the books of the company, not exceeding, however (except to the extent that earned surplus shall have been duly capitalized), the net amount received by the new company on the issue thereof; and (3) additional property, or additions and betterments acquired by the use of the capital fund hereinafter provided for shall not be eligible as a basis, in whole or in part, for the issue of bonds. Whenever any bonds shall be issued, or deposited cash withdrawn, on the basis of the acquisition of new equipment or to provide cash for such acquisition, an equipment sinking fund shall be established under which the new company will pay in cash to the trustee under the new first mort-

gage, on January 1 and July 1 of each year from available net income as hereinafter described, an installment of sinking fund equal to the quotient determined by dividing the principal amount of such bonds or the amount of cash so withdrawn by twice the number of years embraced in the original effective service life of such equipment, in no case to exceed fifteen, less the number of years of effective service life of the equipment which have elapsed since it was placed in service. Moneys held in such sinking fund shall be applied to the retirement of such bonds or of any new first-mortgage bonds as specified in the new first mortgage, by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders or, to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. No bonds shall be issued on the basis of the acquisition of equipment under equipment-trust obligations or any obligations for the deferred or serial payment of purchase price, or on the basis of the retirement of any such obligations.

A sinking fund shall be provided for retirement of first-mortgage series A bonds to be issued in the reorganization, the annual payments to be equal to one-half of 1 percent of the largest principal amount of such bonds at any time previously authenticated and delivered, including bonds under pledge, such payments to be made if the available net income for the previous year is sufficient therefor after payment of all fixed charges, prior contingent interest, and payment into the capital fund, but before payment of contingent interest. Such payments shall not be cumulative. The sinking fund shall be applied to the retirement of first-mortgage series A bonds by purchase at not exceeding the current redemption price plus accrued interest, or by redemption. All first-mortgage bonds of series A so acquired shall be canceled, and no bonds of any kind issued to refund them.

The first mortgage shall contain a covenant substantially to the effect that the excess of the aggregate principal amount of all first-mortgage bonds under pledge at any one time, over the principal amount of all indebtedness so secured, shall not exceed 10 percent of the aggregate principal amount of all first-mortgage bonds then authenticated and uncanceled.

The new first mortgage shall provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof, and of any or all supplements thereto, and of the rights and obligations of the new company thereunder and of the holders of the bonds at any time, by the concurrent action of the new company and of the holders of not less than two-thirds in aggregate

principal amount of the bonds then outstanding affected by such change or modification; provided that no such change or modification shall *(a)* alter or impair the obligation of the new company to pay the principal or interest of any bond at the time and place and at the rate and in the currency provided therein without the consent of the holder of such bonds, *(b)* permit the creation by the new company of any mortgage or lien in the nature of a mortgage ranking prior to or on a parity with the lien of the new first mortgage, except as in the new first mortgage otherwise expressly provided unless the creation of such mortgage or lien be consented to by the holders of all outstanding bonds, or *(c)* alter the specific provisions herein made for sinking funds nor the following provision with respect to the postponement of interest, without approval by this Commission. Notwithstanding the limitation in clause *(a)* in this paragraph, the obligation of the new company to pay interest on bonds issued in the reorganization for presently outstanding securities (and any other bonds as to which it may be so provided in the mortgage or any supplemental indenture) may be modified by the concurrent action of the new company and of the holders of not less than three-fourths in aggregate principal amount of such bonds then outstanding, so as to postpone the time of payment of any particular installments of interest, or any described number of installments of interest, until any fixed or determinable date or until the happening of any specified contingency, not in any case later than the date when the principal of such bonds shall be or become payable; but no postponement shall be made of any installment of interest in excess of a cumulative total of 10 semiannual installments excluding installments paid or as to which due provision for payment has been made; and before any such postponement becomes effective the holders of such bonds shall become, and until all postponed installments of interest be paid or due provision for payment thereof be made shall remain, entitled to elect the smallest number of directors necessary to constitute a majority of the full board.

New income-mortgage bonds.—E. The new income mortgage shall constitute a lien subject only to the lien of the first mortgage and any liens that may at the time be prior to the lien of the first mortgage, upon all property from time to time subject to the lien of the first mortgage.

The income mortgage shall contain an appropriate provision in such terms as the reorganization committee shall determine, that the trustees under the mortgage may at any time release from the lien of the mortgage any of the mortgaged property no longer required in the operation of the property and that the proceeds

from any sale or disposition thereof shall be equally and to the same extent held subject to the lien of the mortgage, as was the property so sold or disposed of.

The income-mortgage bonds may be issued in series, all equally secured as to principal and interest. Approximately $29,750,184 of series A income bonds shall be issued in the reorganization in partial settlement of claims, and additional bonds as may be necessary for the purpose of pledge, as provided in the plan. Additional bonds of other series shall be issuable without limit as to amount, or within such limit as may be specified in the mortgage, having such dates, maturities, rates of contingent interest, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission.

Such additional bonds shall be issuable on such bases, including the refunding of debt and the deposit of cash, as shall be prescribed therein, provided that (1) bonds may be issued on the basis of additional property, including new equipment free from any other lien, and additions and betterments only to the extent of 75 percent, less prior lien debt, of the net amount of such additional property or additions and betterments, computed on the basis of cost, including prior lien debt, thereof or value thereof to the new company, whichever may be less; and (2) additional property, except equipment free from any other lien, or additions and betterments acquired by the use of the capital fund, hereinafter provided for, shall not be eligible as a basis, in whole or in part, for the issue of income bonds. Whenever any income bonds shall be issued, or deposited cash withdrawn, on the basis of the acquisition of new equipment or to provide cash for such acquisition, an equipment sinking fund shall be established under which the new company will pay out of available net income, as hereinafter provided, to the trustee under the new income mortgage on January 1 and July 1 of each year an installment of sinking fund equal to the quotient determined by dividing the principal amount of such bonds or the amount of cash so withdrawn by twice the number of years embraced in the original effective service life of such equipment, in no case to exceed 15, less the number of years of service rendered by the equipment since first placed in service. Moneys held in such sinking fund shall be applied to the retirement of such bonds or of any new income-mortgage bonds as may be specified in the new income mortgage, by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders or, to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. No bonds shall be

issued on the basis of the acquisition of equipment under equipment-trust obligations or any obligations for the deferred or serial payment of the purchase price, or on the basis of the retirement of such obligations.

The series A income-mortgage bonds to be issued in the reorganization shall have a term of 75 years and shall bear interest at the rate of 4½ percent per annum, payable annually. Such interest shall, within the limits of the accumulation hereinafter specified, become absolutely due as a debt on its due date each year in respect of the income period ending the next preceding December 31. Interest on the series A income-mortgage bonds shall, however, be mandatorily payable, except as otherwise provided by the last sentence in this paragraph, only out of available net income of the new company in respect of such income periods or, in the case of accumulations of interest, out of available net income in respect of such income periods or subsequent income periods; the board of directors of the new company may, however, in its discretion, cause the payment of interest on the bonds out of any funds whatever that may be lawfully available therefor. Interest on the outstanding income bonds, excluding bonds held in the sinking fund, shall be paid if covered by available net income, and, if not fully covered thereby, then to the extent so covered, in multiples of one-fourth of 1 percent; any available net income remaining undistributed shall, to the extent of the interest for such income period on the income bonds that accrued but was not paid, be held in the treasury of the new company and added to the available net income for the next succeeding income period. Interest on the series A income-mortgage bonds shall be cumulative to a maximum due at any one time of 18 percent of their principal amount, whether such amount represents interest for consecutive or nonconsecutive income periods. Accumulations of interest shall not bear interest. In case of accumulations of interest, the earliest due coupons or installments of interest shall be paid first. When the principal of any of the income bonds shall become payable, whether at maturity or upon redemption or by acceleration or in any other manner, or a permanent or confirmed appointment shall be made of any trustee or receiver for the new company or its property, all accumulated interest on such bond or bonds shall become immediately and absolutely payable regardless of earnings.

The series A income-mortgage bonds shall be redeemable, in whole or in part, on any interest payment date, on 30 days' notice by publication, at their principal amount plus interest at the rate of 4½ percent per annum accrued since the next preceding first day of April plus any unpaid accumulated interest. They shall be

entitled to the benefit of a sinking fund to be created by the payment on April 1 of each year of an amount equal to one-fourth of 1 percent of the aggregate principal amount of such bonds issued. Such payments shall be payable only out of available net income after payment, or setting aside for payment, of all accumulations of interest and of the full interest requirements at the rate of 4½ percent per annum for the applicable income period on the income bonds outstanding. Such payments for the sinking fund shall be cumulative to a maximum number at any one time of five installments, whether consecutive or non-consecutive installments. Moneys in the sinking fund shall be applied to the retirement of the series A bonds by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders and, to the extent not so applied, then, if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. The bonds so purchased or redeemed shall be held alive in the sinking fund and shall continue to bear interest for the purposes of the sinking fund, and interest payable thereon, calculated at the rate paid for the applicable income period, including accumulations, on outstanding bonds, shall be added to the installments of sinking fund above provided for. No income-mortgage bonds shall be issued in lieu of the income bonds so purchased or redeemed for the sinking fund.

The new income mortgage shall provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof, and of any or all supplements thereto, and of the rights and obligations of the new company thereunder and of the holders of the bonds at any time, by the concurrent action of the new company and of the holders of not less than two thirds in aggregate principal amount of the bonds then outstanding; and such modification or alteration may specifically include procedural provision for ascertaining available net income without the maintenance of separate books of account in the event that the new company shall be merged or consolidated or unified with a new company to result from the reorganization of The Western Pacific Railroad Company or with any other corporation; provided, however, that no such change or modification shall *(a)* alter or impair the obligation of the new company to pay the principal of or accumulated interest on any bond, or to pay interest on any bond out of available net income, as determined by the provisions hereof, or by any such alteration or modification of such provisions, at the time and place and at the rate and in the currency provided in such bond without the consent of the holder, of such bond, or *(b)* permit the creation by the new company of any mortgage or lien in the nature of a

mortgage ranking prior to or on a parity with the lien of the new income mortgage except as in the new income mortgage otherwise expressly provided, unless the creation of such mortgage or lien be consented to by the holders of all outstanding income bonds, or alter the provisions herein stated for sinking funds for the retirement of income bonds.

The income mortgage shall contain a covenant substantially to the effect that the excess of the aggregate principal amount of all income-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured shall not exceed 10 percent of the aggregate principal amount of all income-mortgage bonds then authenticated and uncanceled.

Restrictions on additional mortgages, et cetera.—F. The new company shall not, without the consent of the holders of at least two-thirds in amount of the preferred and common stocks, voting as separate classes, (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new first mortgage and new income mortgage, hereinbefore mentioned, and purchase-money liens, including equipment-trust liens, upon property hereafter acquired, given for not more than 75 percent of the purchase price of such property; (2) purchase or acquire, or contract to purchase or acquire, any property, or system of properties, at a cost to the new company of $5,000,000 or more, in cash or principal amount of par or book value of securities; (3) make any loans in an aggregate amount exceeding at any one time the aggregate amount of $200,000 to any subsidiary or parent or affiliated or other interest except by way of purchase of bonds of such borrower and pledge thereof under the new first mortgage subject to the conditions and restrictions to be provided therein; (4) merge or consolidate with any other corporation or dispose by sale or lease or otherwise of its assets as an entirety or substantially as an entirety; or (5) make any amendment to its charter or certificates of incorporation affecting the rights or interests of such stockholders.

In the event the new company shall be merged or consolidated or unified with a new company to result from the reorganization of The Western Pacific Railroad Company, or with any other corporation, then by vote or consent of two-thirds in par value of the preferred stock then outstanding procedural provision may be made for ascertaining available net income without the maintenance of separate books of account, and such provision shall be binding on all holders of stock of such class.

Determination and application of available net income.—G. The first mortgage and the income mortgage shall make appropriate

provision for the determination and application of available net income and a capital fund as follows:

The available net income of the new company shall be determined for each calendar year ending December 31. The available net income for each such income period shall equal the remainder left after deducting from the income of the new company arising from the properties subject to the lien of the new income mortgage and from the properties or systems acquired by the new company under the plan which is available for fixed charges for such income period (determined in accordance with the accounting rules of this Commission at the time in force or other analogous Federal authority having jurisdiction at the time, or, to the extent not covered by such accounting rules, in accordance with sound accounting practice) such part of the following amounts as arise in the operation of, or are incident to, the aforesaid properties; namely:

(a) All fixed charges, determined in accordance with such accounting rules or practice of the new company accrued during such income period, including fixed interest payments on the Salt Lake first-mortgage bonds and income bonds in the event consolidation with the Salt Lake is effected under the plan; provided, however, that, if in any income period the new company shall fail to earn such fixed charges, the amount of such deficit may, in the discretion of the board of directors of the new company (and shall in the event that funds shall have been borrowed because of such deficit to pay such fixed charges), be paid out of income for the next ensuing period or periods before determining available net income, and any income so deducted before determining available net income shall be first used to retire any indebtedness that may have been incurred for the purpose of paying such fixed charges;

(b) All other charges properly deductible from such income in determining income after fixed charges under such accounting rules or practice, but excluding contingent interest and sinking fund requirements, hereinafter provided for;

(c) The sum, subject to the proviso set out below, of 2½ percent of total railway operating revenues (determined in accordance with such accounting rules or practice) of the new company for such income period, subject to a maximum limit of $750,000 for each 12-month period, which sum shall constitute the capital fund and be disposed of as hereinafter set forth. Any amount by which such income in any income period shall be inadequate to provide for the capital fund, i. e., shall fall below 2½ percent of total railway operating revenues, subject to the aforesaid maximum, shall accumulate and be carried forward, as an additional requirement of the capital fund, into the next succeeding income period, but not

beyond; provided that payments into the fund in any calendar year shall not exceed the sum necessary to bring the total in the fund to $1,500,000 after all withdrawals from the fund during the same year as hereinafter provided for; and

(d) All payments to sinking funds which may have been established, as provided above, for the retirement of first-mortgage bonds issued for the acquisition of equipment free of other lien.

The available net income for each income period shall be applied to the following purposes and in the following order:

(1) All available net income shall, to the extent required, and subject to the provision hereinbefore made for payment in even multiples of one-fourth of 1 percent and postponement of fractional surplus, be applied to the payment, on April 1 in each year, of prior contingent interest at the rate of 1 percent per annum, pro rata on the first-mortgage bonds, series A, of the new company then outstanding and on the modified Salt Lake income bonds outstanding, in the event of consolidation with the Salt Lake; otherwise on the first-mortgage bonds of the new company only.

(2) Any then remaining available net income shall be applied to the payments to sinking funds, if any, which may have been established for the retirement of income bonds issued for the acquisition of equipment free of other liens.

(3) Any then remaining available net income shall be applied on April 1 of each year to the general sinking fund for retirement of the first-mortgage bonds, series A, as specified under section E of this order.

(4) Any then remaining available net income shall, to the extent required and subject to the provision hereinbefore made for payment in even multiples of one-fourth of 1 percent and postponement of fractional surplus, be applied in the payment on April 1 of each year to interest on the then outstanding income-mortgage bonds of the new company, excluding bonds then held in the sinking fund under the new income mortgage, but including bonds under pledge, accruing during the income period ending on the next preceding December 31, and to the payment of any unpaid accumulated interest on said bonds.

(5) Any then remaining available net income shall be applied, until all the income bonds of the new company shall have been retired, on April 1 in each year to a sinking fund for such bonds in an amount up to, but not exceeding, in respect of any income period, one-fourth of 1 percent of the total principal amount of income bonds issued, plus an amount equal to the interest on income bonds theretofore purchased or redeemed for the sinking fund, calculated at the rate paid, pursuant to the foregoing clause

(4), in respect of such income period, including accumulations, upon outstanding income bonds. Any amount by which the available net income remaining for such purpose is inadequate to pay the full amount of such installment of sinking fund shall be cumulated within the limits hereinabove stated and added to the installments payable in the next ensuing income period or periods.

(6) Any then remaining available net income shall be applied to payment to the sinking fund to be created and paid to the trustee under the first mortgage in the event the principal amount of first-mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either *(a)* 45 percent of the total capitalization of the new company, determined as elsewhere provided in the plan on the basis of consolidation with the Salt Lake, or 40 percent without such consolidation, or *(b)* the result obtained by deducting the principal amount of funded debt, other than first-mortgage bonds, bearing contingent interest, from 65 percent of the total capitalization at the time outstanding.

(7) Any then remaining available net income shall be applied, as may be declared by the board of directors, to the payment of dividends in the order of their priority or to other proper corporate purposes.

The available net income for any period after December 31, 1942, until the new company comes into ownership and possession of the properties of the companies embraced in the plan, or of their trustees in bankruptcy, shall be computed as if the new company had come into such ownership and possession on January 1, 1943, and had issued, as of that date, the new securities issuable under the plan and had assumed obligation with respect to interest on the Salt Lake bonds.

Capital fund.—H. The above provisions for the deduction of the capital fund from the income of the new company available for fixed charges are subject to the following proviso: If the new company shall establish and maintain, in such manner as may be permitted or required by law or lawful regulation, an operating expense account for depreciation of its roadway and structures, then *(a)* the capital fund shall be paid from the reserve for depreciation on roadway and structures so credited in respect of the applicable income period to the extent that the amount so credited to said depreciation reserve shall be adequate therefor; *(b)* to that extent the foregoing provisions for the deduction of the capital fund shall cease to be operative; and *(c)* the new company shall not be entitled to withdraw any moneys from the capital fund until it shall have expended in the current calendar year for additions and betterments properly chargeable to capital account under

said accounting rules or practice more than the amount by which its charge for depreciation of roadway and structures in such year, less cash expenditures incurred in the making of retirements properly charged to the depreciation reserve so credited, exceeds the total paid into the capital fund in such year and then only to the extent of such excess.

The capital fund shall be accumulated through the deposit of funds on April 1 of each year and shall, subject to the proviso in the next preceding paragraph, be withdrawable by the new company to reimburse it for, or to provide for:

(a) All of the cost, payable in cash, of additions and betterments to the mortgaged property, including equipment, which are properly chargeable to capital account under said accounting rules or practice, and not previously certified or thereafter to be certified to the trustee under the new first mortgage as the basis, in whole or in part, for the issue of additional new bonds, or the release of mortgaged property or the withdrawal of cash held by such trustee, and further provided that no expenditures so used as a basis for the withdrawal of any moneys from the capital fund shall be made the basis for the issue by the new company of any form of indebtedness or stock ranking prior to or on a parity with the new preferred stock;

(b) All of the amount by which the unfundable purchase price, as hereinafter defined, for new equipment exceeds equipment depreciation surplus, as hereinafter defined. In the case of equipment acquired under equipment-trust obligations, the unfundable purchase price shall equal the initial or down payment for such equipment. In the case of equipment acquired and paid for by the withdrawal of deposited cash under either of the new mortgages, the unfundable purchase price shall equal that part of the purchase price not so withdrawable. Equipment depreciation surplus shall equal the remainder determined by deducting (1) the total installments of principal of equipment-trust obligations or other obligations for the deferred or serial payment of the purchase price for equipment, and installments of equipment-sinking funds paid out of equipment depreciation, as hereinabove provided in the next preceding income period, from (2) the total charges to operating expenses in such income period for depreciation of equipment. Such withdrawals from the capital fund shall be permitted only on the basis of such payments for equipment made or to be made in the calendar year in which the payment of such moneys into the capital fund is due; and

(c) For the purpose of paying fixed interest on the bonds outstanding under the new first mortgage in a year or years in which

the net earnings of the new company available for interest on said bonds shall be inadequate for the payment of such interest, and only to the extent of such inadequacy.

New stock issues.—I. The preferred stock of the new company shall be authorized in the total amount of 500,000 shares, of the par value of $100 each, of which approximately 325,312 shares shall be issued in the reorganization, excluding shares which shall be issued for pledging purposes. Such stock shall be entitled to receive dividends out of available net income as hereinabove provided, or out of earned surplus from prior income periods, when and as declared by the board of directors of the new company, at the rate of 5 percent per annum in respect of each calendar year beginning January 1, 1943, before any dividends shall be paid or declared or set apart for payment on the common stock. Such dividends shall be cumulative to the extent earned in respect of any income period but not paid, but such dividends shall otherwise be noncumulative. In any liquidation or winding up or distribution of the assets of the new company, whether voluntary or involuntary, the new preferred stock shall be entitled to receive, out of the assets of the new company, its par value plus any accrued and unpaid cumulative dividends thereon, before any distribution shall be made to any common stock, but shall not be entitled to any further participation in any such assets. The new preferred stock shall be redeemable in whole or in part at any time at its par value plus accumulated and unpaid dividends and proportionate dividend for the current year. The new preferred stock shall be convertible at the option of the holder at any time, except that stock which is called for redemption shall be convertible not later than 15 days prior to the date as of which such call shall be made, into new common stock at the rate of 1 share of common stock for each share of preferred stock.

The common stock of the new company shall be authorized in the total amount of 1,000,000 shares, having a par value of $100 a share, and approximately 351,676 shares shall be issued in reorganization, excluding shares to be pledged, and approximately 325,312 shares shall be reserved for conversion of the preferred stock.

The preferred stock and common stock shall have equal voting rights, each share being entitled to one vote in the election of directors and in all matters of proprietary interest; provided, however, that the holders of the preferred stock, voting as a class, shall always have the right to elect not less than one-third, and in no event less than two, of the members of the board of directors. Cumulative voting shall be permitted.

Treatment of claims and distribution of new bonds, stock, et cetera.—J. In the event that consolidation of the Salt Lake properties is to be effected as provided herein; the Reconstruction Finance Corporation shall receive, in payment of the debtor's and secondary debtor's notes to it, with accrued interest to December 31, 1942, $5,200,000 of new first-mortgage bonds and $8,700,605 of new income bonds plus the amount of the rental or other use and occupation claim of the Salt Lake Western trustee against the principal debtor's trustees which may be allowed by the court. Upon receipt of such new securities, the Reconstruction Finance Corporation shall deliver to the reorganization committee all the securities now held under pledge.

Nothing contained herein shall be construed as limiting in any manner affecting the right of the Finance Corporation to apply, in its discretion, the income on and the proceeds of the collateral held by it to or toward the payment of the principal or interest, or both, to or upon its claim against the debtor prior to the consummation of the reorganization.

In the event consolidation of the Salt Lake is not to be effected as herein provided, the claim of the Reconstruction Finance Corporation shall be provided for as follows: For the $1,445,000 of Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $10,000 of Rio Grande Western Railway Company first trust 4-percent bonds, $1,395,000 of the Rio Grande Western Railway Company consolidated-mortgage 4-percent bonds, and $4,385,000 of the debtor's refunding and improvement mortgage 5-percent bonds, pledged as part security for the loans, the Reconstruction Finance Corporation shall be entitled to receive $1,566,846 of new first-mortgage bonds, $1,388,150 of new income bonds, $3,181,757 of new preferred stock, and $3,861,910 of new common stock. These new securities, together with the $1,266,600 of Denver & Salt Lake income bonds, 500 shares of Goshen Valley stock, $1,777,000 of Rio Grande Southern first-mortgage bonds, 73,710 shares of Denver-Colorado Springs-Pueblo Motorway stock, 2,262 shares of Rio Grande Motorway stock, 45,889 shares of Denver & Salt Lake stock, and 36,310 shares of Salt Lake Western stock, now held in pledge, shall be deposited under an escrow agreement with a bank or trust company designated by the court, and escrow receipts therefor shall be issued to the Reconstruction Finance Corporation. The agreement shall be for a term of 6 years, and shall provide that the escrow agent (1) shall, at the request of the Reconstruction Finance Corporation, sell all or any part of the deposited securities at such price or prices as may be stated in the request, subject in the case of the sale of the stock of

the Denver & Salt Lake, and of the Denver & Salt Lake Western, to anyone other than the new company, to the approval of this Commission both as to the sale and as to the price to be paid, and (2) shall impound any or all receipts from the deposited securities, whether from sale, dividends, or interest, and make payments of same promptly to the Reconstruction Finance Corporation which shall agree to credit such receipts first against the interest accrued on the claim of $12,900,605 from January 1, 1943, to date at the rate of 4 percent per annum, and further agree to apply any funds received in excess of such interest requirement to reduction of the principal of the claim; *provided, however,* (1) that the new company shall have the right to purchase at any time all of the stock of the Salt Lake, or of the Salt Lake Western, which the Reconstruction Finance Corporation shall have requested the escrow agent to sell, at the price or prices stated in such request; (2) that if, prior to the expiration of the escrow agreement, the total sum paid through the foregoing means to the Reconstruction Finance Corporation shall equal the total amount due on the claim with accrued interest, the securities remaining in the hands of the escrow agent, together with any cash on hand after settlement of the said debt, shall forthwith be turned over to the new company; and (3) that, if at the expiration of the escrow agreement, the claim of the Reconstruction Finance Corporation shall not have been discharged in full, all the securities remaining on deposit, together with any cash balance, shall be turned over to the Reconstruction Finance Corporation in final settlement of its claim, subject, however, to the right of the new company, prior to such transfer, to acquire all of such securities by payment of the balance then due on the Reconstruction Finance Corporation claim, including interest.

It shall be provided that the Reconstruction Finance Corporation shall be bound by the terms of any sale or sales to which it has consented and which have been approved by this Commission. During the life of the escrow agreement, the Reconstruction Finance Corporation shall have the right to receive notice of all meetings of the holders of stocks under deposit and to direct the escrow agent as to the manner in which stocks represented by the escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stocks shall be voted in such manner as the escrow agent may determine. The reasonable compensation and expenses of the escrow agent shall be paid by the new company.

The money value of any award for the rental or other use and occupation claim of the Salt Lake Western trustee against the principal debtor's trustees, as allowed by the court, shall be paid

over to the Reconstruction Finance Corporation and the amount of the claim, or of the face amount of any note evidencing the indebtedness, correspondingly reduced without otherwise affecting the foregoing provisions with respect to the discharge of the claim where consolidation is not to be carried out.

K. The holders of bonds of the classes shown below shall receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, substantially the following amounts of new securities:

Rio Grande Western Railway Company first-trust bonds, $970.20 of new first-mortgage bonds and $349.80 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $266.00 of new income bonds, $970.90, par value, of new preferred stock, and $93.10, par value, of new common stock; Rio Grande Junction Railway Company first-mortgage bonds, $1,061.96 of new first-mortgage bonds and $317.21 of new income bonds; Denver & Rio Grande Railroad Company consolidated mortgage 4-percent bonds, $318.92 of new first-mortgage bonds, $217.08 of new income bonds, $321.60, par value, of new preferred stock, and $482.40, par value, of new common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $329.03 of new first-mortgage bonds, $223.97 of new income bonds, $331.80, par value, of new preferred stock, and $497.70, par value, of new common stock; the debtor's refunding and improvement mortgage 5-percent bonds, $250.01 of new first-mortgage bonds, $159.61 of new income bonds, $310.75, par value, of new preferred stock, and $692.13, par value, of new common stock; the debtor's refunding and improvement mortgage 6-percent bonds, $264.61 of new first-mortgage bonds, $168.94 of new income bonds, $328.90, par value, of new preferred stock, and $732.55, par value, of new common stock; and the debtor's general mortgage bonds, $146.10, par value, of new common stock.

The interests or equities of (1) all general unsecured creditors of the debtor whose claims are not entitled to priority over the mortgages of the debtor, (2) holders of preferred stock of the debtor, and (3) holders of common stock of the debtor have no value and nothing shall be distributable to them.

Scrip shall be issued for sums less than $100 in the case of bonds, and for fractional shares of stock.

The trustee under the Rio Grande Western Railway Company consolidated mortgage shall be permitted to obtain the release of the equities in the stock of the Utah Fuel Company and distribute the stock among the holders of the aforesaid bonds in any manner

agreeable to them, or to enforce its rights as pledgee of the stock of the Utah Fuel Company, the proceeds recovered to be distributed to the holders of the bonds.

The new company shall pay, in cash, all interest coupons on the bonds or equipment obligations of the debtor or its subsidiaries other than the Denver and Salt Lake Railway Company which had been declared payable but had not been paid prior to November 1, 1935, if and when such coupons are presented by the holders thereof.

There shall be set aside, for securities issued in the reorganization of 1924 which have not been claimed, new securities under the plan herein approved to the same extent as for like outstanding securities of the debtor, or those claims shall be settled in cash as may be determined by the court.

The secured note held by the Chase National Bank shall be canceled, and a new note or new notes issued in face amount equal to that of the present note, plus interest accrued to January 1, 1943, in the amount of $2,158,458, or such other amount as may be allowed by the court, such notes to mature in 10 years, and to bear interest at the rate of 4 percent per annum, payable semiannually on October 1 and April 1 of each year, but such interest shall be contingent on, and payment thereof shall be limited to, the total of the interest and dividends paid by the new company on the collateral securing such notes. The interest shall be cumulative to the maximum amount at any one time of 16 percent (whether for consecutive or nonconsecutive income periods). Any interest and/or dividends paid upon the pledged collateral in excess of interest requirements on such notes (including accumulations of interest) shall be applied to the payment of the principal amount of such notes. Such notes may be redeemed in whole or in part at any time on 30 days' notice at their principal amount plus full interest at the rate of 4 percent per annum accrued since the last preceding April 1, and all unpaid accumulated interest. Upon the payment or other retirement of all such notes, the collateral securing them shall be returned to the new company, and the new company shall, in the case of certificates of stock, cancel and retire the same, and in the case of bonds deliver the same forthwith to the trustee under the indenture securing the same for cancelation and retirement; no bonds shall be issued in lieu of any bonds so canceled and retired. The new securities issuable as collateral shall consist of not exceeding $1,524,076 of new first-mortgage bonds, $972,998 of new income bonds, $1,894,332 of new preferred stock, and 42,192 shares of new common stock.

The proposal to be submitted to the holders of the Salt Lake

income bonds; constituting the terms upon which consolidation of the Salt Lake shall be carried out, shall be that (1) the maturity of such bonds shall be extended to that of the first-mortgage series-A bonds to be issued by the new company, and (2) that the interest terms of the present bonds be modified to provide for fixed interest at the rate of 3 percent per annum and fully cumulative prior contingent interest at the rate of 1 percent per annum, and both payable when fixed and prior contingent interest, respectively, are payable on the new first-mortgage bonds, subject to the right of the new company, as in the case of the new first mortgage, described above, to postpone the payment of installments of interest by the concurrent action of the new company and the holders of not less than three-fourths of the total amount of income bonds outstanding. The proposal shall be presented to the bondholders in the form determined by the reorganization committee, and the committee shall report the results to the court. If the holders of 90 percent or more of the income bonds outstanding shall accept the proposal within 90 days of its submission to them, the consolidation of the Salt Lake properties with the debtor's properties shall be carried out, as herein provided. The reorganization committee shall be authorized to call for payment any Salt Lake income-mortgage bonds the holders of which shall not have assented to the proposed modification of terms, or to arrange for the refunding or purchase of such bonds, at the convenience of the new company.

In the event of consolidation with the Salt Lake on the basis herein provided, the new company shall assume all the obligations under the two Salt Lake mortgages, as stated therein in case of a merger into any other company, including the assumption of the obligation with respect to the payment of the principal and interest of all bonds now outstanding, except as the terms of the Salt Lake income bonds shall be modified, as provided above. No additional bonds shall be issued under either of the Salt Lake mortgages. The new company shall also assume the present tunnel contract, and the trackage agreement shall be canceled.

The holders of stock of the Salt Lake outstanding in the hands of the public shall, in the event the merger or consolidation of that railroad is effected under the plan, be entitled to receive therefor the preferred stock of the new company on the basis of one share of such stock for each share of Salt Lake stock.

In view of possible changes in the amounts of the obligations herein shown as outstanding, the reorganization committee shall be authorized, in order to give effect to such changes, to make such adjustments in the claims provided for in the plan, and such

changes in allotment of securities, consistent with the provisions of the plan, as may be approved by the court.

New financing.—L. Any cash that may, in the judgment of the reorganization committee, be needed in reorganization, but in no event to exceed $2,000,000, shall be advanced by the Reconstruction Finance Corporation or obtained through private channels and evidenced by collateral note of the new company for a term of 12 years, secured by pledge of new first-mortgage bonds in an amount equal to 125 percent of the loan, or such other amount of bonds as may be required by the lender and approved by this Commission. As an alternative to such a loan, not exceeding $2,500,000 of new first-mortgage bonds may be issued for sale to provide the new money required, under terms and conditions to be determined by the reorganization committee and approved by the court and this Commission.

Voting trust for new stock.—M. All the preferred stock and all the common stock, issued by the new company in reorganization, excepting shares issued to qualify directors, shall be deposited under an escrow agreement with a bank or trust company designated by the court, and escrow receipts issued to persons entitled to receive such stock under the plan. The escrow agreement shall be for a term of 10 years from the date of creation of the trust, such term to be considered as beginning not later than 6 months after confirmation of the plan, and shall provide that the reorganization committee, as voting trustees, may, subject to the approval of the Commission, and with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of preferred stock on deposit, sell all or any part of such preferred stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders; likewise the voting trustees may sell all or any part of the deposited common stock, with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of such common stock.

It shall be provided that all holders of escrow receipts shall be bound by the terms of any sale or sales which shall have been approved by this Commission and consented to as aforesaid, and the net proceeds of any sale or sales, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts for preferred stock and common stock, respectively, according to the class of stock sold. During the life of the escrow agreement, the holders of escrow receipts shall have the right to receive notice of all meetings of stockholders and to direct the voting trustees as to the manner in which the stock represented by the escrow receipts shall be voted at such meetings. In the absence

of such directions, the deposited stock shall be voted in such manner as the voting trustees may determine. The reasonable compensation and expenses of the voting trustees, including counsel fees, shall be paid by the new company.

Directors.—N. The number of directors of the new company and the manner of their election shall be determined by the reorganization committee and provided in the new charter or an amendment of the debtor's present charter.

Leases, agreements, et cetera.—O. In the event consolidation of the various companies, including the Salt Lake, shall be effected, as herein provided, the new company may take any action with respect to the lease or agreement with the Northwestern Terminal Railroad Company as may be lawful under the terms thereof. As to all other agreements and executory contracts, including the existing lease agreement of the Salt Lake with the Moffat Tunnel Improvement District, the new company shall be deemed to have assumed the obligations with respect to such agreements and contracts which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding and which shall not have been disaffirmed by the trustees of the respective estates with the approval of the court prior to confirmation of the plan, and the new company shall also assume any executory contracts made by the trustees, with the approval of the court, which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding.

In the event consolidation of the Denver & Salt Lake is not effected, the foregoing provisions with respect to the lease agreements with the Northwestern Terminal Railroad Company and the Moffat Tunnel Improvement District shall not apply, and the assumption of obligation by the new company with respect to agreements and contracts shall be confined to those entered into with the debtor and its affiliated companies but not those entered into with the Denver & Salt Lake but not with the debtor.

Claims against the debtor and its subsidiaries entitled to priority over their respective mortgages, claims for taxes levied, assessed, or accrued against the debtors, their subsidiaries, or trustees, current liabilities and obligations incurred by the trustees during the reorganization proceedings, to the extent unpaid at the date of confirmation of the plan, and claims arising from the disaffirmance of executory leases or contracts of the trustees pursuant to orders of the court, in respect of which claims are filed or evidenced in accordance with orders of the court, shall be assumed by the new company, and paid in the usual course of business with the same

relative priority as they now have with respect to other obligations of the debtor or its subsidiaries.

Expenses of reorganization.—P. The expenses of reorganization, as allowed by the court, subject to the provisions of section 77, shall be paid in cash.

Reorganization committee.—Q. A reorganization committee shall be created which shall carry out the plan under the supervision and control of the court. It shall consist of five members, two to be designated by the insurance group committee as representatives of the Rio Grande Western first-mortgage bonds, the Junction first-mortgage bonds, the Denver & Rio Grande consolidated-mortgage bonds, and the Rio Grande Western consolidated-mortgage bonds, one to be designated jointly by the trustee under the debtor's refunding and improvement mortgage and the trustee under the debtor's general mortgage, one by the Reconstruction Finance Corporation as its representative, and one by the judge of the United States District Court for the District of Colorado. Should any of the parties named fail to designate its representative or representatives, as the case may be, within such time as the court shall consider reasonable, the court shall appoint such representative or representatives. The reorganization committee may fill any vacancies created by death, resignation, or otherwise, preserving the representation of the several interests as before. The members of the committee as such, shall agree to serve without compensation, but its expenses shall be paid by the new company, subject to the provisions of section 77 and the approval of the court, as part of the cost of the effectuation of the plan. In their capacity as voting trustees, the members of the committee shall be entitled to compensation and expenses as provided above in connection with the voting trust.

The reorganization committee shall have, subject to any requirements of law and the requisite approval of the court and this Commission, full and plenary discretionary power to take all such action and to enter into such arrangements, financial and otherwise, as they may deem necessary or advisable in order to consummate and carry into execution the plan or any modification thereof; to create a new corporation if a new corporation be deemed advisable; to supervise and determine the form of instruments necessary to transfer the property of the debtor to the reorganized corporation; to employ and fix the compensation of mortgage trustees, depositaries, counsel, and others whose services they may employ in the execution of their powers; to determine the form and provisions, so far as not otherwise herein specifically provided, of the certificate of incorporation of the new company, if a new cor-

poration is to be formed, and its bylaws, or to determine the necessary amendments to the debtor's certificate of incorporation and its bylaws, the new bonds and the mortgages and trust agreements under which the same shall be issued, the stock certificates, and any other instruments deemed by the reorganization committee to be necessary or proper in connection with the plan; to provide the method by which creditors and other interested parties may participate in the plan; and to do all other acts in their discretion advisable for carrying out the plan.

The court shall, before they are put in use, approve the articles of incorporation, amendments to articles of incorporation, bylaws, mortgages, trust agreements, bonds, securities, stock certificates, and the escrow agreement for the new stock.

Except as otherwise expressly provided in the plan, the reorganization committee may act by a majority at a meeting, or by unanimous consent in writing without a meeting; they may, from time to time, delegate to others any power or discretion conferred upon them by the plan; and its members shall not be liable for any action taken by them in good faith or by any person employed by them in good faith, except for their respective individual malfeasance or willful neglect.

The reorganization committee shall not be authorized to solicit authorizations to represent security holders, or solicit the deposit of securities for purposes other than exchange, except upon approval by this Commission of the terms of such solicitation, pursuant to section 77 (p) of the Bankruptcy Act.

Acceptance of the plan shall include acceptances of the new bonds, mortgages, stock certificates, and all instruments necessary and appropriate to the carrying out of the plan, other than the orders of the court and this Commission, to the same effect as though the terms of such instruments were set out in full herein.

The method by which creditors and any other parties in interest may, after confirmation of the plan by the court, participate therein shall be determined by the reorganization committee with the approval of the court, and notice thereof duly given.

Provision permitting sale of debtor's property.—R. If so ordered by the court, the plan, after it has been found fair and equitable and confirmed by the court, may be executed by the sale or sales, at not less than fair upset prices, to be fixed by the court, of all or any part of the property of the debtor and the secondary debtor, all on such conditions and in such manner as the court may direct. Upon any such sale or sales, the property and assets offered for sale may be purchased for the benefit of the new company by the reorganization committee, and in that event there shall be applied

on account of the purchase price the distributive share of the proceeds of such sale of all securities the holders of which shall have assented to the plan, and of the securities, though not assenting to the plan, of all classes which shall have accepted the plan. If the property of the debtor or secondary debtor, or both, so offered for sale should be sold to others than the reorganization committee, the plan herein approved shall be deemed inoperative except insofar as provision is made therein for the sale of the properties as may be ordered by the court.

In the event of any such sale to the reorganization committee, it may in its discretion sell all or any portion of the new securities distributable under the plan in respect of securities of any creditor, if neither such creditor nor the class to which such creditor belongs shall have accepted the plan, provided that creditors, in a class which shall not have accepted the plan, and who themselves shall not have accepted the plan, shall have the right, if they shall so notify the committee within a period of 30 days after the confirmation of the sale to assent to the plan and receive the securities allocated to them under the plan in lieu of their aliquot share of the proceeds of such sale. The proceeds of sale of securities, with the approval of the court, and any other funds which in the judgment of the reorganization committee are available among the assets of the debtor's estate and are not necessary for the working capital requirements of the new company, or to pay any of the obligations under the plan, may be used to pay the portion of the purchase price payable in cash on any such sale of the properties.

Taxes due to the United States.—S. The debtor, as reorganized, or the transferee of the property, shall assume the liability for, and shall pay in full in due course, any and all taxes due to the United States from the debtor or the trustees for any taxable period prior to the date of confirmation of a plan of reorganization, without requiring proof thereof in this proceeding and without prejudice by reason of not having been proved herein, subject, however, to the statutes of limitation normally applicable to the assessment and collection of such taxes, provided, however, that the liability of the reorganized company for any taxes which are the subject of litigation on the date of the confirmation of the plan of reorganization, or which may become the subject of litigation on any date thereafter and prior to the expiration of the applicable statute of limitations, shall be determined pursuant to law, and provided, further, however, that this provision shall not be deemed to preclude either the debtor, the trustees, or the reorganized company from contesting the merits of any such tax in the manner provided by law.

Construction of plan.—T. The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively.

Additiondl Clauses from Commission's Order of June 14, 1943

In addition to the provisions of the plan approved hereinbefore shown, the Commission's order approving the plan also ordered—

(1) That the authorization and approval herein granted by this Commission are upon the condition that the journal entries covering the necessary accounting adjustments under the order will be submitted to this Commission for approval before they are recorded on the books of the new company under the plan of reorganization herein approved.

(2) That nothing herein contained shall be, or be construed as, a grant of authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation, or merger of the debtor's property, or pooling of traffic pursuant to either the Bankruptcy Act or the Interstate Commerce Act, except as provided herein, or until further action by this Commission upon confirmation of the plan by the court; and

(3) That, except as aforesaid, the petitions for modification of the report and order of July 13, 1942, be, and they are hereby, denied.

PLAN OF REORGANIZATION

Change Made by the Court in the Plan of Reorganization Approved by the Commission

On September 16, 1943 the court entered an order directing the trustees to purchase the Rio Grande Junction bonds at par and accrued interest at 5 percent per annum from June 1, 1935 from all bondholders tendering their bonds for purchase and the trustees have given notice pursuant to the order that on and after November 1, 1943 they will purchase such bonds at said price, but with accrued interest terminating on that date.

In the above-described order the court referred to the provision of the plan approved by the Commission providing that the provisions of the plan with respect to the Rio Grande Junction bonds should be considered as separable. It appearing that the above action of the court was taken pursuant to such provision, and that the plan in so far as it provides treatment for the Junction bonds will not be placed in effect, no submission will be made of the remainder of the plan to the Junction bondholders.

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002[1]

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted December 7, 1938. Decided July 11, 1939

Plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, approved.

F. C. Nicodemus, Jr., and *William V. Hodges* for debtors.

Henry W. Anderson, George D. Gibson, Leighton H. Schurbeck, Oscar R. Ewing, Harry Hoffman, Edgar J. Goodrich, Mildred E. Reeves, John B. Marsh, Edward E. Watts, Jr., Fred N. Oliver, Karl Michelet, Charles J. Nasmyth, John E. Benton, Clyde S. Bailey, Simon Fleishman, Clarence R. Freeman, Stanley Marsh, Robert McKinney, W. Heyward Myers, Jr., Philip B. Fisher, William Clarke Mason, Edwin S. S. Sunderland, Thomas O'G. FitzGibbon, Malcolm Fooshee, Daniel Willard, Jr., Gerald Hughes, William A. W. Stewart, Harry L. Umbarger, Erskine R. Myer, James B. Alley, C. C. McChord, C. M. Clay, W. Meade Fletcher, Jr., Arthur A. Gammell, W. C. Roper, Jr., H. Struve Hensel, Frederick W. Wood, Rodney J. Bardwell, Jr., H. H. Larimore, Russell L. Dearmont, W. M. Dyer, Carl Giessow, C. O. Heinley, Paul B. Cromelin, and *H. C. Clark*, for interveners.

Report of the Commission

BY THE COMMISSION:

Exceptions to the report[2] proposed by the examiner were filed, and oral argument was heard. Our conclusions differ from those of the examiner.

[1] This report also embraces reorganization and consolidation of the Denver & Salt Lake Western Railroad Company, secondary debtor, the Denver & Salt Lake Railway Company, the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company, none of the last three having filed petitions under section 77.

[2] Previous reports, 212 I. C. C. 105 and 709, 217 I. C. C. 101, and 224 I. C. C. 574. Orders entered without report (other than order permitting interventions) January 21, August 8, and September 4, 1936; January 9, April 12, May 26, and October 27, 1937; and May 26 and November 28, 1938.

The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company, hereinafter referred to as the Denver and the Salt Lake Western, or the debtor and the secondary debtor, respectively, on November 1, 1935, filed petitions with the District Court of the United States for the District of Colorado, stating that they were unable to pay their debts as they matured and that they desired to effect a plan of reorganization under section 77 of the act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. On the date of the filing of the petitions the court entered orders approving the petitions as properly filed and, among other things, pending the appointment of trustees, authorized and directed the debtor to operate and maintain both properties, under the supervision of the court. Copies of the petitions and the orders thereon have been transmitted to us by the clerk of the court. In like manner we have received lists of all known creditors and stockholders of the debtors, together with copies of orders of the court determining the time within which and the manner in which the claims and interests of the creditors and stockholders may be filed or evidenced and the division of creditors and stockholders into classes for the purpose of the plan and its acceptance. These and other documents similarly received are now of record in the proceeding before us.

By order entered November 18, 1935, the court appointed Wilson McCarthy and Henry Swan trustees of the debtor, and these appointments were later ratified by division 4. By order entered December 19, 1935, the court appointed Raymond L. Sauter trustee of the secondary debtor, and this appointment was likewise ratified. Upon petition of the debtors, the court on April 29, 1936, entered an order extending the time for filing a plan of reorganization from the due date under section 77(d) of the act to and including August 1, 1936. On July 29, 1936, a "Proposed Plan of Consolidation and Reorganization as of January 1, 1937" was filed with the court and with us by the debtors. The plan embraced the Denver, the Salt Lake Western, the Denver & Salt Lake Railway Company, the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company.

By the provisions of section 77(d), after the filing of a plan, unless such plan is found to be *prima facie* impracticable, we are required to hold public hearings thereon, at which any interested party may be heard, and to render a report and order in which we may either approve or refuse to approve a plan. The plan approved may be different from any which has been proposed but it must in our opinion, among other things, be fair and equitable, afford due

recognition to the rights of each class of creditors and stockholders, not discriminate unfairly in favor of any class of creditors or stockholders, conform to the law of the land regarding the participation of the various classes of creditors and stockholders, and be compatible with the public interest. After due notice, hearings were held in October 1936 and in February, April, and June, 1937. At the hearing on June 15, 1937, a plan of reorganization embracing the companies covered by the debtor's plan was filed by the Insurance Group committee, an intervener, of which George S. Van Schaick was chairman. Besides this group the interveners included the trustees under certain mortgages, the Untermyer family group, the Security Research Bureau, the Chase National Bank of the City of New York, the Railroad Credit Corporation, several chambers of commerce and boards of trade, the Reconstruction Finance Corporation hereinafter called the Finance Corporation, and others. Briefs were filed.

Classes of creditors and stockholders.—The district court, by order entered November 23, 1936, divided the claims and interests of the creditors and stockholders as follows: Class 1, common stock; class 2, preferred stock; class 3, claims entitled to priority under section 77 (n); class 4, claims which would have been entitled to priority over existing mortgages or other liens if a receiver in equity had been appointed for the property; class 5, claims not included in classes 3 and 4, which are entitled to priority by virtue of the laws of any State or of the United States; class 6, bonds issued under the consolidated mortgage of the Denver & Rio Grande Railroad Company dated July 15, 1886, assumed by the debtor; class 7, bonds issued under the first-trust mortgage of the Rio Grande Western Railway Company, dated July 1, 1889, assumed by the debtor; class 8, bonds issued under the first consolidated mortgage of the Rio Grande Western Railway Company, dated April 1, 1899, assumed by the debtor; class 9, bonds issued under the first mortgage of the Rio Grande Junction Railway Company dated December 1, 1889, assumed by the debtor; class 10, bonds issued under the debtor's refunding and improvement mortgage dated February 1, 1924, and bonds issued under the improvement mortgage of the Denver & Rio Grande Railway Company, dated June 1, 1888, which may be held to be pledged under the aforesaid refunding and improvement mortgage; class 11, bonds issued under the debtor's general mortgage dated February 1, 1924, and bonds issued under the improvement mortgage of the Denver & Rio Grande Railroad Company which may be held to be pledged under the aforesaid refunding and improvement mortgage; class 12, secured notes of the debtor held by the Railroad Credit Corporation,

the Chase National Bank of the City of New York, and the Finance Corporation, and the debt of the Salt Lake Western, represented by the debtor's demand note which was pledged by the Salt Lake Western as security for a loan from the Finance Corporation; and class 13, all other claims not coming within any of the aforesaid specific classifications.

Claims evidenced by equipment-trust indentures and leases, or equipment-trust certificates secured thereby, were not classified, in view of the following provision of section 77 (j):

> The title of any owner, whether as trustee or otherwise, to rolling stock equipment leased or conditionally sold to the debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this section.

The amount of stock, bonds, secured notes, and unsecured claims outstanding will be shown in detail later.

The Properties

The Denver's principal eastern termini are Denver and Pueblo, Colo., at each of which points connection is made with the Atchison, Topeka & Santa Fe Railway and the Colorado & Southern Railway. At Denver connection is also made with the Chicago, Burlington & Quincy Railroad, the Chicago, Rock Island & Pacific Railway, and the Union Pacific Railroad; at Pueblo, also with the Missouri Pacific Railroad, which is the Denver's main outlet to the east.

On the west the main line of the Denver passes through Salt Lake City and terminates at Ogden, Utah. Connection is made with the Union Pacific at each point; at Salt Lake City the Denver also connects with the Western Pacific Railroad and at Ogden with the Southern Pacific. The interchange with the Western Pacific is more important than that with any other western connection.

The road owned by the Denver consists of 1,256.6 miles of main line and 1,094.9 miles of branch lines. Operated under lease are the Rio Grande Junction Railway (hereinafter called the Junction) extending from Rifle to Grand Junction, Colo., 62.1 miles, the Goshen Valley Railroad, a branch line 8.8 miles in length, and the Salt Lake Western, extending from Dotsero, on the Denver, to Orestod on the Denver & Salt Lake Railway (hereinafter called the Salt Lake), 38.1 miles. Including these leased lines, the Denver operates approximately 1,357 miles of main lines and 1,104 miles of branch lines. Approximately 771 miles of narrow-gage lines are included in the operated mileage.

In addition to the above-mentioned mileages, the Denver operates over the Salt Lake, between Denver and Orestod, 128.6 miles. This line, together with the Salt Lake Western, constitutes the Dotsero cut-off route. The Salt Lake's ownership embraces the line extending from Utah Junction, near Denver, to the western terminus at Craig, Colo., 220.2 miles. For its Denver terminal, the Salt Lake uses, under a lease, the facilities of the Northwestern Terminal Railroad Company. The Salt Lake derives no revenues from the through traffic moving over the cut-off, since all such traffic is handled by the Denver.

The present Denver Company was organized on November 17, 1920, succeeding the Denver & Rio Grande Railroad Company, organized in 1908. The former corporation acquired the property of the Rio Grande Western Railway Company (hereinafter called the R. G. Western), owning the line extending west from Crevasse, Colo., to Ogden, Utah, and that of the Denver & Rio Grande Railroad Company of 1886, owning all lines east of Crevasse except the Junction line. The 1908 company assumed obligation in respect of bonds issued under the R. G. Western's first-trust mortgage of 1889 and its first consolidated mortgage of 1899. It likewise assumed obligation in respect of bonds issued under the first consolidated mortgage made by the Denver & Rio Grande of 1886.

The Denver & Rio Grande Railroad Company of 1908 also assumed the obligations of the predecessor companies with respect to securities issued by the Western Pacific Railway Company. It also issued bonds under new mortgages, viz., the first and refunding mortgage and the adjustment mortgage. Default in the payment of interest on the first-mortgage bonds of the Western Pacific led to a deficiency judgment against the Denver of 1908 and ultimately to the creation of the present Denver Company, which assumed obligation for all the bonded debt of the former company. It issued 309,000 shares of capital stock to the Western Pacific Railroad Corporation, a new company formed for the purpose of controlling the Western Pacific Railroad Company. See *Denver & R. G. W. R. Co. Stock*, 70 I. C. C. 102. Later a half interest in this stock was sold to the Missouri Pacific Railroad Company for $9,000,000. *Acquisition of Denver & R. G. W. Common Stock*, 90 I. C. C. 161.

Operation of the Junction property under lease began in 1890 and continues under the same lease. It originally provided for the guaranty of the Junction's first-mortgage bonds of 1889 by the Denver of 1886 and the Colorado Midland Railway Company. The latter ceased operation in 1918. These bonds constitute an obligation of the present debtor. The debtor owns $906,000 of the Junc-

tion's refunding junior bonds, issued in 1929, and $2,000,000, par value, of the Junction's capital stock.

The debtor owns the entire capital stock of the Goshen Valley, having a par value of $50,000.

Foreclosure proceedings were instituted against the Denver in 1922 as a result of default in the payment of interest on the first and refunding mortgage and the adjustment-mortgage bonds, issued in 1908, which were undisturbed in the previous reorganization. A receiver was appointed and the property was sold at auction to the reorganization managers in accordance with the plan of June 15, 1923. By deed dated December 1, 1924, the property was conveyed back to the company. See *Denver & R. G. W. R. Co. Reorganization*, 82 I. C. C. 745 and 90 I. C. C. 141. The aforesaid first and refunding mortgage bonds, purporting to represent a lien on a substantial amount of equipment, were exchanged 60 percent in new general-mortgage bonds and 40 percent in preferred stock.

The Salt Lake was incorporated on November 3, 1925, and on January 1, 1927, acquired the properties of the Denver & Salt Lake Railroad Company at foreclosure. *Denver & S. L. Ry. Co. Reorganization*, 117 I. C. C. 397.

The latter company had by similar means acquired the properties of the Denver, Northwestern & Pacific Railroad Company in 1913, and has extended the line from Steamboat Springs to Craig, approximately 41 miles. Owing to difficult operating conditions, the carrier went into receivership in 1917. Between that time and the reorganization of 1925-26, the Moffat Tunnel project was carried out by the Moffat Tunnel Commission, which manages the property of the Moffat Tunnel Improvement District. The tunnel is 8.9 miles in length, and the portion built for railroad use is leased to the Salt Lake. Under the terms of this lease the Salt Lake is obligated to pay 66⅔ percent of the principal and interest of the Moffat Tunnel bonds, the cost of maintaining the railroad tunnel, and certain other amounts. The Moffat Tunnel Improvement District, pointing out that it has no relations with the Denver Company and that a consolidation of the Salt Lake with the Denver in connection with the reorganization would cause the former, now solvent, to lose its corporate identity, contends that the Salt Lake has no right to assign or sublet the lease of January 6, 1926, without the consent of the tunnel district. It suggests that if the present lease is to be canceled provision should be made for a new lease with the consolidated company under which the tunnel district will receive the same measure of security that it now has from the present lessee.

With the purpose of developing a western outlet, the Salt Lake

organized the Salt Lake Western, which completed the construction of its line from Bond, near Orestod, to Dotsero on June 15, 1934, pursuant to the certificate issued by the Commission in *Denver & S. L. W. R. Co. Construction*, 154 I. C. C. 51 and 175 I. C. C. 535. All the capital stock of the Salt Lake Western was owned by the Salt Lake. Along with the granting of authority for the construction of the Salt Lake Western line, the Commission authorized the Denver to acquire control of the Salt Lake by purchase of capital stock; *Denver & S. L. Ry. Co. Control*, 170 I. C. C. 4, and 175 I. C. C. 542. Later, in *Denver & R. G. W. R. Co. Operation*, 189 I. C. C. 129, it authorized the Denver to operate the line of the Salt Lake Western under lease and to operate under trackage rights over the line of the Salt Lake between Utah Junction and Orestod. The agreements made by the carriers in respect of these matters are described in *Denver & S. L. W. R. Co. Construction, supra*. The agreement relating to the Salt Lake Western provides that, contingent upon the transfer of that company's stock or mortgage bonds to the Denver, the latter would finance the construction of the cutoff. The terms of the lease were also set forth. In accordance with this agreement, $3,631,000, par value, of the stock of the Salt Lake Western was transferred to the Denver. The Salt Lake Western has issued no bonds.

The total amount of stock of the Salt Lake acquired by the Denver is 49,540 shares of no-par value. Stock remaining outstanding in the hands of the public aggregates 460 shares. All the stocks of the Salt Lake and the Salt Lake Western owned by the Denver, together with various other securities, are pledged with the Finance Corporation as collateral security for loans for the financing of the construction project, the acquisition of the Salt Lake stock, and the payment of interest, taxes, and maturing equipment-trust certificates.

The investment in road and equipment of the several corporations, as shown on the consolidated balance sheet of December 31, 1936, was as follows: $211,635,295 for the Denver, $5,328,626 for the Junction, $3,659,578 for the Salt Lake Western, $503,890 for the Goshen Valley, and $17,059,350 for the Salt Lake, a total of $238,186,739. Including all investments, the grand total was $240,145,360. As of December 31, 1935, the grand total was $238,759,511.

In connection with the above-stated amounts appearing on the consolidated balance sheet, the debtor introduced an analysis of capitalizable assets, based on data furnished to us in other proceedings in connection with applications for authority to issue securities. The result arrived at is $241,295,293, which is described

as the grand total capitalizable investment as of December 31, 1935.

The report of the Bureau of Valuation dated March 1, 1937, filed in this proceeding by direction of division 4, sets forth various elements of rate-making value in respect of the Denver property and that of its subsidiaries, as of December 31, 1935. For the Denver the original cost is $142,800,512, the cost of reproduction new $168,729,747, the cost of reproduction new, less depreciation, $115,467,756, the value of lands and rights $5,428,159, and the amount of working capital $2,473,400. For the Salt Lake the corresponding amounts are $17,549,593, $19,934,420, $14,462,618, $91,854, and $287,000. For the Junction, omitting working capital, the amounts are $3,401,673, $4,100,037, $3,409,074, and $60,330, for the Goshen Valley $499,441, $308,078, $270,756, and $1,908, and for the Salt Lake Western $3,547,081, $3,920,258, $3,880,723, and $7,219, respectively. The totals for the system are original cost $167,798,300, reproduction cost new $196,992,540, reproduction cost new, less depreciation, $137,490,927, land and rights $5,589,470, and working capital $2,760,400.

The sum of the last three amounts is $145,840,797, and if net additions and betterments during 1936 be added thereto the total would be $147,717,268. On the basis of original cost the total as of December 31, 1936, would be $178,024,641.

Securities of the Denver which are owned by the Western Pacific Railroad Corporation include 150,000 shares (50 percent) of no-par common stock, $2,070,000, par value, of preferred stock, $1,000,000 of refunding and improvement mortgage bonds, $3,751,875 of general-mortgage bonds, $364,000 of R. G. Western first consolidated mortgage bonds, and $10,000 of the first consolidated mortgage bonds of the Denver of 1886. Most of these securities are pledged, the Denver's common stock being deposited with the Finance Corporation as security for a loan to the Western Pacific Railroad Company.

Securities of the Denver which are owned by the Missouri Pacific include 150,000 shares (50-percent) of the no-par common stock, $608,800, par value, of the preferred stock, and $1,000,000 of refunding and improvement mortgage bonds. All the common and preferred stock is pledged with the Railroad Credit Corporation.

Proceedings for the reorganization of the Western Pacific and Missouri Pacific under section 77 are pending before us and the courts.

Present capital structure.—The Denver's balance sheet of December 31, 1936, shows common stock (300,000 shares) as $62-

457,540, preferred stock $16,445,600, funded debt unmatured $76,707,500, trustees' certificates $650,000, and grants in aid of construction $800,313. Total current assets were $8,025,321 and total current liabilities were $69,729,998, the latter including $12,966,372 of interest matured unpaid and $45,317,500 of funded debt matured unpaid. Corporate surplus was shown as a deficit of $2,309,419 in liabilities.

The debtor's common stock is held under a trust agreement dated February 1, 1924, voting-trust certificates being held in equal amounts by the proprietary companies. The preferred stock is entitled to dividends at the rate of 6 percent per annum, cumulative from February 1, 1924, and to $100 a share in a dissolution of the company, in preference to the common stock. No dividends have ever been paid on this stock. Equipment-trust certificates were outstanding as follows: Series A, $600,000; series B, $575,000; and series C, $630,000. Pursuant to the authority granted by division 4 in *Denver & R. G. W. R. Co. Trustees' Equipment Trust Certifs.*, 221 I. C. C. 291, $2,175,000 of series-D certificates were issued by the trustees in 1937. The equipment-trust certificates outstanding on June 30, 1938, consisted of $345,000 of series B, $420,000 of series C, and $2,030,000 of series D, a total of $2,795,000.

The Denver's long-term funded debt outstanding as of December 31, 1936, is briefly described as follows: Junction first-mortgage 5's due December 1, 1939, principal amount $2,000,000, unpaid interest $158,333; R. G. Western first-trust 4's due July 1, 1939, principal amount $15,190,000, unpaid interest $1,215,200; D. & R. G. first consolidated mortgage bonds due January 1, 1936, consisting of $34,125,000, principal amount, of 4's, with unpaid interest of $3,412,500, and $6,382,000 of 4½'s, with unpaid interest of $717,975; R. G. Western first consolidated 4's due April 1, 1949, principal amount $15,080,000, unpaid interest $1,357,200; the Denver's refunding and improvement mortgage bonds, consisting of series A, due October 1, 1974, principal amount $2,000,000, unpaid interest $270,000, and series B, due April 1, 1978, principal amount $12,000,000, unpaid interest $1,350,000; and the Denver's general-mortgage 5's, due August 1, 1955, principal amount $29,808,000, unpaid interest $12,544,200, of which $7,452,000 represents noncumulative interest to February 1, 1929, included in the total claim as stated by the trustee under the mortgage.

In addition to the foregoing there have been issued and pledged $906,000 of the Junction's refunding 5's, $10,000 of R. G. Western first-trust 4's, $1,395,000 of R. G. Western consolidated 4's, $1,445,000 of D. & R. G. first consolidated 4's, and $10,481,000 of the

Denver's refunding and improvement mortgage 5's. A statement of all securities pledged for short-term loans appears later.

The debtor introduced statements setting forth its views as to what properties are subject to the respective first liens of the several mortgages. The Junction's first mortgage and refunding mortgages represent first and second liens, respectively, on the 62.1 miles of line owned by this company. No equipment is involved with these mortgages. The R. G. Western first-trust mortgage represents a first lien on 314 miles of main line and a total of 415 miles of line, together with equipment having a ledger value, less depreciation, of $17,637, as of December 31, 1936. The R. G. Western first consolidated mortgage represents a second lien on that property and a first lien on approximately 283 miles of branch lines in Utah, the entire capital stock of the Utah Fuel Company, and equipment having a ledger value, less depreciation, of $681,191. The D. & R. G. first consolidated mortgage represents a first lien on 875 miles of standard-gage lines and 683 miles of narrow-gage lines in Colorado, and on equipment having a ledger value, less depreciation, of $4,708,523, as considered by the debtor. The Denver's refunding and improvement mortgage represents a first lien on 85 miles of standard-gage and 34 miles of narrow-gage branch lines in Colorado and Utah, a junior lien on all other lines owned, and a first lien on equipment having a ledger value, less depreciation, of $7,268,622, according to the debtor. In addition, there are pledged under this mortgage the shares of stock, less directors' qualifying shares, of the Junction, the Denver Union Terminal Company, the Pueblo Union Depot & Railroad Company, and the Salt Lake City Union Depot & Railroad Company owned by the debtor, together with $906,000 of the Junction's refunding bonds. The Insurance Group committee argues that a portion of the above-mentioned equipment, having a depreciated value of $1,333,252, should be allocated to the first lien of the D. & R. G. first consolidated mortgage rather than to that of the refunding and improvement mortgage, as the trustee of the latter contends. This question will be discussed later. The Denver's general mortgage represents a lien generally upon the property securing the refunding and improvment mortgage but junior thereto. The Denver's investment in the stocks and bonds of the R. G. Western, the Salt Lake, the Salt Lake Western, and the Goshen Valley, together with advances, aggregates $15,060,147. Its short-term secured debt, as of December 31, 1936, consisted of loans from the Finance Corporation totaling $10,691,850, upon which the interest unpaid amounted to $628,108, a balance of approximately $300,000 due on a loan of $500,000 from the Railroad Credit Corporation, and a demand

note for $1,500,000 given to the Chase National Bank of the City of New York upon which $53,948 of interest was computed by the debtor and the committee up to December 31, 1936.

The collateral pledged as security for the Denver's note to the Finance Corporation in the amount of $7,581,000 and the Salt Lake Western's note in the amount of $3,110,850 (the latter also secured by a demand note of the Denver for $3,182,150) consists of the following securities: $10,000 of R. G. Western first-trust 4's, $1,395,000 of R. G. Western first consolidated 4's, $783,000 of D. & R. G. first consolidated 4's, $4,385,000 of the Denver's refunding and improvement 5's, $1,266,000 of the Salt Lake's income 6's, 49,546 shares of the Salt Lake's capital stock, 36,310 shares of the Salt Lake Western's capital stock, 56,700 shares (100 percent) of the capital stock of the Denver–Colorado Springs Pueblo Motor Way, Incorporated, 1,352 shares (100 percent) of the capital stock of Rio Grande Motor Way, Incorporated, 500 shares (100 percent) of the capital stock of the Goshen Valley Railroad Company, and $1,777,000 of bonds of the Rio Grande Southern Railroad Company. The above-stated shares of the motor companies' stock include additional shares deposited in May 1937 in accordance with the supplemental certificate issued by division 4 in *Denver & R. G. W. R. Co. Reconstruction Loan*, 221 I. C. C. 107. The notes to the Finance Corporation are further secured by a junior lien on the collateral pledged with the Railroad Credit Corporation and the Chase National Bank, viz, $662,000 of D. & R. G. first consolidated 4's and $6,096,000 of the Denver's refunding and improvement 5's, respectively. The Credit Corporation is further secured by pledge of the debtor's distributive share of the funds collected under the marshaling and distributing plan and by a junior lien on the collateral pledged with the Finance Corporation. The motor companies above referred to represent an investment of $172,300 by the Denver. Operating as feeders to the railroad, they report substantial earnings in practically every year since 1927.

Unsecured general claims against the debtor aggregated approximately $440,000. An undetermined amount falls within the six-months rule. To the extent these unsecured creditors are not paid off currently they would be offered, under the debtor's plan, participating preferred stock at the rate of one share for each $100 of claims.

The debtor stated that, during the 11-year period following the previous reorganization, more than $30,000,000 was expended on the property for additions and betterments, while the amount of equipment obligations was reduced by $1,925,000 and the amount of refunding and improvement mortgage bonds outstanding was

increased by $12,000,000, due, however, chiefly to the retirement of bonds matured on June 1, 1928. For the payment of interest and taxes not earned in 1931, 1932, and 1933, loans of $3,950,000 from the Finance Corporation and of $500,000 from the Railroad Credit Corporation were obtained. Additional loans from the Finance Corporation, in the amounts of $3,631,000 and $3,110,850, were obtained for the Salt Lake Western construction and the purchase of Salt Lake stock, respectively. The bank loan of $1,500,000 was also applied to the latter purpose. Including $1,042,559 of Salt Lake income bonds, together with advances, the Denver's investment in the cut-off route amounts to $12,526,376.

Division 4, by orders entered on January 29 and December 23, 1937, and March 1, 1938, authorized the trustees of the debtor to issue and sell trustees' certificates of series C not exceeding $1,800,000 in amount, series D not exceeding $3,200,000, series E not exceeding $1,800,000; and series F not exceeding $2,000,000. *Denver & R. G. W. R. Co. Trustees' Certificates*, 217 I. C. C. 796, and 224 I. C. C. 336 and 596. The series-C certificates were paid at maturity. The series-F certificates were never issued. By order entered January 24, 1939, division 4 authorized the trustees to issue and sell $5,000,000 of series-G certificates for the purpose of paying a like amount of outstanding certificates at maturity, early in February, 1939. The series-G certificates bear interest at the rate of 3½ percent, mature on February 1, 1942, and are redeemable on any interest-payment date at par and accrued interest. 230 I. C. C. 609.

The Denver's obligation in respect of the securities of the three terminal companies, mentioned above in connection with the refunding and improvement mortgage bonds, is shown in the agreements made for joint use of the terminals. Copies of the balance sheets and income accounts of the terminal companies are of record herein. The debtor's trustees have advised us that they and the trustees of the Western Pacific were unable to pay the $557,000 of first-mortgage bonds of the Salt Lake City Union Depot & Rail-Road Company which became due on November 1, 1938, and for which the Denver and the Western Pacific are jointly liable under a four-party agreement dated November 1, 1908. This agreement has not been adopted by the trustees of the debtors, but they have met the interest and sinking-fund payments on the terminal bonds when due. They propose to refinance the major part of the matured bonds with the aid of the Finance Corporation.

The unpledged securities then owned by the debtor and its subsidiaries included $46,000 of certificates issued by the receiver of the Rio Grande Southern Railroad Company and $850,000 of

United States Treasury bonds. The debtor stated that these were the only securities in the list which had any realizable value. The treasury bonds have since passed out of the debtor's possession.

At the hearing it was stated that in connection with the Denver's reorganization of 1924 there were still issuable $108,900 of general-mortgage bonds and $15,600 of preferred stock in exchange for old securities. There were still issuable by the Salt Lake, in connection with its reorganization plan of 1925, approximately $20,200 of bonds and 30 shares of stock, and $21,806 in cash was being held for payment to nonassenting bondholders of the predecessor company. Counsel for the trustees have advised us that as of April 30, 1939, the securities of the Denver held for conversion of old securities consisted of 124 shares of preferred stock and $24,950, principal amount, of general-mortgage bonds. It appears that in the final decree of sale of the property in 1924 the holders of the old refunding bonds and adjustment bonds are entitled to their distributive share in cash (estimated at about $8,568) and that the refunding-mortgage trustee has sought an order of the court in the old receivership proceeding to authorize such settlement. The outcome of this matter cannot be determined at this time.

As has been stated, the capitalization of the Salt Lake Western consists of common stock, all of which is owned by the debtor. The securities of the Salt Lake outstanding consist of 50,000 shares of common capital stock of no-par value, of which 49,540 shares are owned by the debtor, and $12,500,000 of funded debt unmatured. The latter amount is composed of $1,500,000 of first-mortgage 4-percent bonds due January 1, 1950, and $11,000,000 of 6-percent income-mortgage bonds due January 1, 1960, of which $1,266,000 are owned by the debtor.

The $2,217,000 of first-mortgage 5-percent bonds of the Northwestern Terminal Railroad Company are involved to the extent that under the terms of the lease the Salt Lake pays a portion or all of the interest on such bonds, according to the amount of the railway revenues, and in the event the Salt Lake is consolidated with any other railroad the new company shall pay the full 5-percent interest. Although the debtor's plan proposes that the use of these terminal facilities be discontinued and that the debtor's terminal facilities in Denver be used by the carriers proposed to be consolidated, it provides in its plan for the possible issue of new first-mortgage bonds to refund the terminal-company bonds outstanding.

Combining and summarizing the capital structures of the debtor and its subsidiaries as of December 31, 1936, and omitting intercompany holdings and securities pledged, the total long-term and

short-term debt, including unpaid interest,[3] was $157,056,723, the amount of preferred stock was $16,445,600, par value, and the common stock outstanding consisted of 300,460 shares of no-par value. The total amount of fixed interest charges for this capitalization was $5,835,392 per annum, the contingent interest charges $584,040 per annum, and the preferred-stock dividend requirements $986,736 per annum, all based on the principal amounts outstanding, without consideration of the $14,293,464 of accumulated unpaid interest on secured obligations and the $12,745,340 of accumulated dividends on the preferred stock.

Subsequent to December 31, 1936, the capital structure was changed by the issue of additional equipment-trust certificates and trustees' certificates, as has been shown, and by the further accumulation of unpaid interest on funded debt and loans.

The debtor presented a pro-forma balance sheet for the combined companies as of December 31, 1936, based on their present investments, with intercompany eliminations and adjustments. The capital liabilities shown are those proposed in the debtor's plan. According to this set-up the assets of the new company would consist of total investments of $228,541,993, total current assets of $9,400,095, total deferred assets of $8,495, and total unadjusted debits of $1,443,351. On the liability side, the total capitalization is shown as $119,454,419, including the proposed no-par participating preferred stock at $1 a share. The amount $113,298,420 is set up as reorganization adjustment of capital, bringing the total capital liabilities to $232,752,839. Total current liabilities are $4,277,141, total deferred liabilities $363,210, and total unadjusted credits $2,000,744. Because of the reorganization adjustment made, no corporate surplus appears.

Traffic and earnings.—As shown by traffic-density charts for the years 1935 and 1936, the Denver's freight traffic is fairly uniform in total amount between Denver and Walsenburg, between Pueblo and Dotsero, between Dotsero and Helper, and between Helper and Salt Lake City, the density increasing in this order of districts. East of Helper the movement is predominantly eastbound and between Helper and Salt Lake City predominantly westbound. Most of the coal tonnage, constituting the largest single item of traffic handled, originates around Helper and moves west. Except on small portions of line the traffic of the narrow-gage lines is generally less than 50,000 net ton-miles per mile of road a year. Of the total through traffic in 1935, approximately 40 percent moved over the cut-off. Some of this traffic was created by the opening

[3] Except $7,452,000 of contingent interest on the general mortgage bonds outstanding.

of the new route and therefore does not represent an actual diversion from the old route via Pueblo.

Of the Denver's freight revenues in 1936, 19 percent was derived from products of agriculture, 6 percent from products of animals, 29 percent from products of mines, 6 percent from products of forests, 34 percent from manufactures and miscellaneous, and 6 percent from less-than-carload freight. The commodities constituting the chief items of traffic move, in general, over all the lines. The traffic originating on the principal branches was described in detail. Compared with the revenues of 1929 the largest relative declines have been in the products of mines and in less-than-carload freight. Compared with 1932 the total revenues in all main freight groups have increased, particularly in products of mines and forests, in manufactures and miscellaneous, and in less-than-carload freight.

The Denver's total carload traffic decreased from 330,250 cars in 1929 to 185,111 cars in 1933, then increased each year to a total of 276,968 cars in 1936. The overhead or bridge traffic handled during the year ended June 30, 1935, aggregated 1,402,477 tons, yielding revenues of $5,754,924. In the opinion of the debtor, 4 or 5 years will be required for the full development of the cut-off route. The traffic handled over it is highly competitive in character.

A record of the Denver's interchange of freight with its principal connections from 1924 to 1935 shows that the tonnage received from the Western Pacific exceeds that received from any other line, while the tonnage delivered to the Missouri Pacific exceeds that delivered to any other. In the reverse movement these roads are also important connections. A large tonnage of freight is interchanged with the Union Pacific and Southern Pacific. The Denver's interchange with the Salt Lake is small compared to the interchange with the trunk lines.

Traffic reported as being handled by the Denver, following the opening of the cut-off route, includes that handled over the lines of the Salt Lake Western and the Salt Lake under the operating agreements made with those carriers but does not include that handled in trains operated by the Salt Lake.

Of the total freight revenues of the Salt Lake in 1936, approximately 61 percent was from the traffic in bituminous coal. Other important items were crude oil, gasoline, and cement. The coal originates at several local stations and is hauled principally to Denver. Mines are numerous in the territory served. The number of carloads handled in 1936 exceeded that of any previous year. The same is practically true of the oil and gasoline. The latter originates at Craig and is shipped to Denver, and to points west

via the cut-off. The Salt Lake's total carload traffic decreased from 32,014 cars in 1929 to 15,801 cars in 1933, then increased each year to a total of 35,213 cars in 1936. The number of carloads delivered to connecting carriers in 1936 was 24,207, and the number received from such carriers was 1,288.

The opening of the Moffat Tunnel in 1928 was followed by a marked increase in the earnings of the Salt Lake, and a further increase followed the opening of the cut-off route on June 15, 1934, owing to the rentals paid to the Salt Lake by the Denver. The latter's net railway operating revenues, however, were reduced. Considering the operation of all lines involved, the net loss due to the cut-off, for the 12 months ended June 30, 1935, was computed at approximately $218,000 on the waybill method of allocating revenues adopted by the debtor, allowing a constructive mileage to the cut-off, or at approximately $285,000 on the waybill basis, allowing the cut-off its actual mileage. The methods used for allocating revenues will be explained in connection with the plans filed.

The Denver's total operating revenues were at a maximum of $34,828,669 in 1929, declined to less than half that amount in 1933, and increased to $25,599,309 in 1936 and $8,180,745 during the first four months of 1937. Net railway operating income, however, did not change proportionately, having amounted to $8,528,676 in 1929, $3,357,643 in 1933, and $1,569,814 in 1936. This decline may be ascribed to the steady increase in operating expenses, taxes, and joint-facility rents. The emergency freight surcharges collected in 1932 and 1933, under the authority of the Commission in Ex Parte No. 103, amounted to $380,862, and during 1935 and 1936, under Ex Parte No. 115, to $547,457. Wage reductions made under agreements with organized labor amounted to $851,780 in 1932, $876,876 in 1933, $872,996 in 1934, and $118,024 in 1935. Wages were fully restored on April 1, 1935. The estimated amount of the charges to tax accruals in 1936 on account of the Federal Railroad Retirement Act was $403,479 and on account of the Social Security Act, $135,017.

The Denver reported a nonoperating income of $675,615 in 1935 and $709,590 in 1936. An analysis of the first figure shows the principal subitems to be income from lease of road and equipment $245,241, dividends on the stock of the Salt Lake Western $145,240, and interest on a bearer note of the Salt Lake Western $128,372. After intercompany eliminations, the nonoperating income (including $66,320 as that of the Salt Lake in the same year) amounted to $223,081. Miscellaneous deductions from income aggregated $260,828 in 1935 and $258,547 in 1936. Income of the

Denver available for the payment of interest was $8,938,657 in 1929, $3,497,991 in 1933, and $2,020,857 in 1936. The net income in 1929 was $3,554,110, and the income deficits in 1933 and 1936 were $2,139,757 and $3,911,204, respectively.

The operation of the narrow-gage lines is reflected in the foregoing figures. About 88 percent of the net ton-miles of these lines is within the territory subject to the lien of the D. & R. G. first consolidated mortgage. The system revenues contributed by the traffic handled from and to points on these lines aggregated $1,953,000 in 1934 and $2,017,000 in 1935. The debtor considers that the system revenue derived from the freight traffic originated on the narrow-gage lines about equals the operating loss on such lines.

During each year of the three years ended June 30, 1935, the income of the Denver available for the payment of interest represented approximately 1.12 percent of the average book investment in road and equipment, less accrued depreciation on equipment.

The total railway operating revenues of the Salt Lake declined from the high level of $3,981,131 in 1929 to the low of $1,620,006 in 1934, increasing to $2,234,882 in 1935, and to $2,856,949 in 1936. The corresponding net revenues from railway operations for 1929, 1934, and 1936, were $1,754,484, $805,155, and $918,281, and the net railway operating income $1,679,287, $913,122, and $1,090,810. The emergency freight surcharges on the Salt Lake amounted to a total of $119,121 during the years 1932, 1933, 1935, and 1936. The wage reductions aggregated $50,863, the charges under the Railroad Retirement Act $50,037, and those under the Social Security Act $17,542. The Salt Lake reported net income of $610,069 in 1929, $12,493 in 1934, and $2,455 in 1936.

The combined income accounts of the Denver and the Salt Lake for the years 1927 to 1936, inclusive, with adjustments for intercompany charges and credits, and for an error appearing in the account for 1935, show a downward trend in the income available for interest from 1929 to 1932, a fairly constant level between 1932 and 1935, when it averaged about $3,600,000 a year, and $2,417,746 available in 1936.

The reports of the Bureau of Accounts, filed in this proceeding by order of division 4, show the result of corrections in the carriers' income accounts, 1930 to 1934, inclusive, for accounting not in accordance with our regulations, an adjustment to include income items entered in profit-and-loss account by our permission and a further adjustment to give retroactive effect to the excise tax in connection with the Railroad Retirement Act, effective March 1, 1936, the Social Security Act, effective January 1, 1936, and our order respecting accounting for equipment depreciation, effective

January 1, 1935. The combined effect of these changes is to reduce the average income of the Denver available for the payment of interest from $4,243,563 per annum to $3,521,239 per annum during the period. On the same basis the average available income of the Salt Lake is reduced from $655,771 per annum to $540,395 per annum.

Although the combined total revenues of 1936 were substantially in excess of those of 1935, the net revenues were less largely because of the heavy maintenance program. Maintenance-of-way expenditures for the system increased from $2,752,695 in 1935 to $4,453,359 in 1936; and maintenance-of-equipment expenditures increased from $5,285,329 in 1935 to $7,215,066 in 1936, notwithstanding the abnormally high maintenance expenditures in 1935 as reflected in the adjustments made by the debtor in the earnings for the year ended June 30, 1935, hereinafter discussed.

On the Denver in 1936 operating expenses were charged with $836,614 in connection with capital charges of $1,314,392 for roadway. On the Salt Lake the operating expenses were $248,005 in connection with $668,574 of capital charges.

In 1936 the Denver expended approximately $1,200,000 on maintenance-of-way work deferred from prior years and in connection with improvements. For maintenance of equipment $800,000 was spent under like requirements. The Denver proposed an improvement program for the years 1937, 1938, and 1939, involving a total capital expenditure of $6,179,700 for road and equipment, with operating charges of $4,070,800, and cash requirements of $9,905,200 in connection with such improvements.

The Salt Lake's line has been largely rebuilt during recent years and the amount of deferred maintenance is evidently slight. A witness for the Finance Corporation considers the line to be virtually a new railroad. However, an improvement program for the years 1937, 1938, and 1939 was contemplated by a director of the Salt Lake, under which the expenditures would be $2,194,000 for road and equipment and $693,000 for operating expenses. More than half this outlay would be made for reducing curvature and revising the alinement. The debtor's testimony was to the effect that the expenditures for improvements would have to be continued for two or three years longer in order to bring the Salt Lake up to the standard of the Denver. Incidental to the showing made by the Finance Corporation with respect to the Salt Lake, a study was introduced in which the income available for interest was estimated at $1,449,000 for 1936 on the basis of the Salt Lake's operation as an independent carrier, assuming no further rehabilitation of the line between Orestod and Denver to be necessary.

A study for a determination of the earnings of the Denver and the Salt Lake during a normal year was presented by the president of the Denver, such study indicating that the total railway operating revenues of both roads would be $33,721,189, the total railway operating expenses $23,918,282 (operating ratio 71.49 percent), the net railway operating revenue $6,435,857, and the income available for interest, $6,215,423. In the opinion of the witnesses such results were to be expected in 1939. The debtor's estimate of freight traffic, which was made in collaboration with the officers of two trunk lines that connect with the Denver, was based on a study of the traffic in each principal commodity handled between 1928 and 1936, and the number of carloads, average tonnage, and average revenue per car for a normal year were estimated in the case of each commodity. Consideration was given to business conditions in the local territory and to the trend of production, to the effect of opening the cut-off, and to present and prospective rate levels. A substantial increase in the traffic connected with the mining industry is reflected in the forecast. Operating expenses were based on the total amount of revenues estimated. A continuation of the present scale of wages was assumed. Maintenance expenses for the Denver were fixed at 33 percent of gross revenues, which compares with an average of 35 percent for the years 1925 to 1936 inclusive. For the Salt Lake the ratio was taken at 30.7 percent.

A study of the prospective revenues of the combined lines was also made by a bank officer, testifying as a financial expert in the debtor's interest, who showed that the operating revenues of the Denver since 1933 represented an increasingly large proportion of the operating revenues of all class I roads. By relating the trend of railroad earnings to the number of workers employed in the durable-goods industries, and making certain assumptions as to normal conditions in industry and in railroad rates, the witness arrived at an estimate of $32,559,560 for the total operating revenues of the Denver. Such sum is $1,825,560 in excess of the "normal" revenues shown in the president's forecast.

The debtor selected the 12 months ended June 30, 1935, as the basis for the allocation of earnings to mortgage districts in connection with the development of its plan of reorganization. In this so-called test period, the total railway operating revenues of the system were $21,828,298, the total railway operating expenses $16,485,571, the net railway operating income $3,149,965 and the income available for interest $2,923,024.

These figures were materially changed, as will be shown in describing the debtor's plan, by adjustments made in order to elim-

inate abnormalities in operating conditions during the test period and to establish a level of earnings which would be generally representative, giving effect to the opening of the cut-off route. Thus the income of the Denver assumed as available for interest was increased from $2,084,783 to $2,813,063, and by adding the earnings of the Salt Lake's independent operation, together with the estimated savings under unified operation, the system income available for interest based on the test-period year was placed at $3,926,223. This was the figure used in computing the amounts of new bonds assignable to the present first-lien bondholders on the basis of the respective earnings of different divisions of the system, but in the determination of the amount of future fixed charges permissible still another change of base was introduced viz, the average earnings of 1932, 1933, and 1934. With certain adjustments, this computation indicated $3,687,328 as the income of the system available for the payment of interest.

Debtor's Plan of Reorganization

The debtor's plan, dated July 28, 1936, is based upon a consolidation of the properties of the Denver, the Salt Lake, the Salt Lake Western, the Junction, and the Goshen Valley. The amount, character and distribution of securities to be issued by the new company were determined primarily from earnings. During the course of the hearing the debtor at the request of certain interveners, made additional studies of the earnings of the lines subject to first-lien mortgages, arriving at a distribution of the new securities which differed materially from that originally proposed. On brief, the revised distribution is favored, yet the debtor states that it does not desire technically to amend the original plan.

In order to ascertain the earnings of the several mortgage districts as a basis for the apportionment of new bonds, the debtor adopted a formula or general method, which was applied to the revenues and expenses of the Denver for the 12 months ended June 30, 1935. The Salt Lake was not included in the first step of the analysis, since its mortgages apply to the entire line and its earnings are separate from those of the Denver. Freight revenues of the Denver were divided among the mortgage districts on an average ton-mile basis, and it was considered proper to assign the same mileage to the cut-off route between Denver and Dotsero as that of the old route between those points via Pueblo, although the latter route is approximately 175 miles longer.

It appears from the revised figures, as has been stated, that the operation of the cut-off during the first year resulted in a system loss of approximately $218,000, because of increased transporta-

tion costs despite a substantial increase in through traffic. The effect of the diversion of traffic to this route was to deprive the lines subject to the lien of the D. & R. G. first consolidated bonds of approximately $900,000 of annual revenue, which would otherwise have accrued to such lines if the same traffic had been handled.

Maintenance-of-way expenses were adjusted in a manner intended to show normal conditions over an average period. For the cut-off, much larger expenses than the actual were used. Maintenance-of-equipment expenses were apportioned to engine districts on the basis of equipment mileage, using the years 1933 and 1934 as typical, and certain assumed ratios were employed in dividing the total expenses of locomotive repairs between the freight and passenger services.

For the use of equipment, the charges to each first-lien mortgage were made on the basis of 2 percent per annum applied to the ledger value of the equipment used, less depreciation. The mortgage with a lien on the most equipment represented the district where the smallest use of equipment took place. The use of the 2-percent rate will be referred to later. Yard switching expenses were distributed on a car-mile basis over the different divisions of the system. This method was also followed for maintenance expenses of yards and yard locomotives, station services, and so forth.

The adjustments made in the actual earnings of the Denver during the test-period year consisted principally of a reduction of approximately $714,000 in total maintenance charges, a reduction of $452,618 in nonoperating income, due to intercompany eliminations, of which reduction $65,889 was not specifically explained, and the elimination of $261,570 of miscellaneous deductions from income, of which $10,807 was not explained. To the income of the Denver there were added $182,342 to compensate for the abnormally low earnings from the potato traffic originating in the San Luis Valley, and $83,333 to represent the earnings of the Utah Fuel Company. As a result of all adjustments the income of the Denver available for interest was finally shown as $2,813,063, and the corresponding amount for the consolidated system as $3,926,223.

Objections to the use of the year ended June 30, 1935, as an earnings base were expressed by the trustee of the R. G. Western consolidated mortgage, the trustee of the Denver's refunding and improvement mortgage, the Untermyer family group, and the Security Research Bureau. In general, these interveners urged that the base should reflect conditions after the cut-off route shall have become definitely established.

The entire formula is admittedly open to objection and is largely a matter of judgment. Controversy arose especially in regard to the debtor's treatment of the cut-off, the priority of mortgage liens with respect to equipment, the rental charged for equipment, the segregation of company freight, the allocation of branch-line losses, the adjustment for the higher rate scale on the narrow-gage lines, and the period chosen as representative of earning power.

The debtor revised its first formula in various respects, principally by allocating freight revenues according to actual waybills to the extent records thereof were available, by segregating company freight and including only so much of the cost of handling as was involved where one mortgage district bore the expense of work done by another, by separating train switching from general road operation and by charging the narrow-gage districts with the cost of transferring freight from narrow-gage to standard-gage cars, and vice versa. The test-period basis of earnings, as adjusted, was retained, but the revisions just mentioned resulted in substantial changes in the allocations.

A further revision of the formula showed the effect of computing the earnings of the cut-off operation on a straight mileage basis. This analysis was utilized in part by the committee in preparing its plan, as will be explained.

From the primary distribution of earnings, the ratio of the earnings of each mortgage district to the total was established. These ratios were next applied to the total fixed interest charges considered permissible for the new company. In the detailed computations such charges were taken at $2,598,474, and in the final set-up for the new capital structure they are shown as $2,584,165. The debtor offers further support for the proposed total fixed charges by referring to the average income available for interest during the 3-year period 1932–34, which with certain adjustments was $3,687,328, or 1.42 times the amount of the charges adopted.

After the distribution to each mortgage district of its proportionate share of the proposed new interest charges, such shares were compared with the earning power of each district, as established on the basis of the test-period performance. In the case of certain districts, such as those represented by the Junction first mortgage and the R. G. Western first-trust mortgage, the earnings exceeded the proposed fixed interest charges; in other divisions deficiencies were shown. The surpluses were passed on to the next junior obligations, and were considered in fixing the amount of new bonds to be offered to the present bondholders, the Finance Corporation, and the Credit Corporation. The Finance Corporation, by virtue of its lien on the stocks of the Salt Lake and Salt

Lake Western, was credited with the earnings of the cut-off route and those of the Salt Lake's separate operation. It was also credited with the dividends paid on the stocks of the motor carriers. From calculations based on the revised formula, the debtor arrived at new proportions for the distribution of first and refunding mortgage bonds, general-mortgage bonds, and first preferred stock to the holders of the present securities. The record of market prices of the debtor's securities was given some weight in determining the allocation of new securities.

The debtor proposes to leave the equipment obligations undisturbed to call in the Salt Lake's bonds for redemption, to issue bonds under three new mortgages, and to issue three classes of new capital stock, all to be exchanged for existing bonds, stocks, and the notes to the Finance Corporation and Credit Corporation in varying ratios. A new collateral note would be issued to the Chase National Bank. No provision is made in the plan for the trustee's certificates outstanding, which, according to the debtor's principal witness, will be paid at maturity. The Western Pacific and the Missouri Pacific would retain stock control of the new company, but each would relinquish the $1,000,000 of refunding and improvement mortgage bonds which it owns, and in addition each would agree to purchase $1,500,000 of new bonds at par. In connection with the equity in the present common stock, the debtor showed that between 1925 and 1935 approximately $4,383,000 was expended for improvements from net income which might have been applied to dividends on the common stock. A statement of the cost of the improvements made on each mortgage district and on the Salt Lake was supplied for the record.

Under this plan new income bonds are to be offered for the 460 shares of Salt Lake stock outstanding in the hands of the public. The Finance Corporation was expected to underwrite $11,443,680 of new first and refunding mortgage bonds, and to accept $11,317,950 of such bonds as payment of the debt to it.

Accruals of unpaid interest on the present bonds and short-term debt of the Denver, excluding pledged bonds, amounted to $14,293,464 as of December 31, 1936. The debtor makes no provision for interest not earned during the trusteeship, amounting to approximately $4,770,000. Other accrued interest is to be funded in new securities junior in rank to those issued against the principal obligation.

The new capitalization proposed by the debtor, based on the obligations actually outstanding on December 31, 1936, would be as follows: Equipment-trust obligations, $1,805,000; Western Division 3½-percent bonds, representing a first lien on the stand-

bonds, as provided in the plan for the purpose of refunding the first-mortgage and income bonds of the Salt Lake now outstanding.

The new capitalization proposed by the committee, based on the obligations actually outstanding on December 31, 1936, would be as follows: Equipment-trust obligations $1,805,000; first-mortgage bonds, series A, $18,563,533; series B, $52,057,197; income-mortgage bonds, $27,042,895; a collateral note for approximately $1,593,948; preferred stock, $26,403,389, par value; common stock, of no-par value, class A, 349,002 shares; warrants for class-A common stock, 164,456 shares; and warrants for class-B common stock, 200,000 shares; total capitalization approximately $128,179,000, taking the no-par common stock at $1 a share. The above total of first-mortgage bonds includes $6,000,000 of bonds proposed to be issuable to redeem trustee's certificates, to provide for reorganization expenses or working capital, or to be applied to other approved purposes. Securities to be issued and pledged are not included in the above summary. Approximately $58,000 in cash would be paid to the holders of certain divisional bonds as an adjustment of interest rates.

The committee argues that the above-mentioned $6,000,000 of first-mortgage bonds should not be included in the proposed capitalization or fixed interest charges, on the theory that cash would be available to retire the trustees' certificates or the bonds issued against them, or in any event the improvements recently made would result in operating economies more than adequate to pay the $240,000 of annual interest on the additional $6,000,000 of new bonds. We think, however, that in any comparison of plans this block of bonds and the interest thereon should be included. In doing this an interest rate of 4 percent will be applied.

On this basis, under the committee's plan, the total amount of fixed-interest debt (omitting the amount due the Railroad Credit Corporation) would be approximately $74,020,000 and the annual fixed interest charges $2,957,000. Contingent interest charges would be approximately $1,217,000 per annum and the dividend requirements on the preferred stock $1,320,000 per annum, not including pledged securities.

The foregoing charges do not include payments to a capital fund up to 2½ percent of total railway revenues, subject to a maximum of $750,000 a year, which is made mandatory under the committee's plan. The committee devoted all of its estimated $2,774,554 of income available for fixed charges to the issue of new first-mortgage bonds, series A and series B. It then computed the allowable amount of contingent-interest bonds from earnings of

about $4,000,000, considered applicable to fixed and contingent interest charges, again disregarding the payment to the capital fund, which, however, is placed before contingent interest.

The theoretical application of income available for interest annually under the committee's proposal would be in the following sequence: (1) Fixed interest; (2) fund for additions and betterments ($750,000); (3) contingent interest; (4) sinking fund for the income bonds ($67,607); and (5) dividends on preferred stock; grand total, before dividends on the common stock, $6,312,000.

Under this plan, the Junction first-mortgage bonds and the R. G. Western first trusts would receive new first-mortgage bonds in amounts equal to the principal of the present bonds, respectively, plus accrued interest. In the case of all other bonds, various proportions of first-mortgage series-B bonds, income bonds, and preferred stock are assigned, except that class-A common stock, only, is to be issued for the present general-mortgage bonds, and the present bonds of the Salt Lake are to be called for redemption and paid through the issue and sale of new first-mortgage series-B bonds, as has been noted. Income bonds in the amount of $9,931 are proposed to be issued to the holders of the 460 shares of Salt Lake outstanding in the hands of the public. The new class-A common stock, allocated to the holders of general-mortgage bonds is to be placed in a voting trust pending the disposal of the matter of equity in the present common stock, as hereinafter explained.

The holders of the 164,450 shares of preferred stock would be offered warrants for the purchase of a like number of shares of new class-A common at a suggested price of $20 a share. The holders of the 300,000 shares of common stock would be offered, pro rata, warrants for 200,000 voting-trust certificates or shares of new class-B common stock at $30 a share, at any time within 6 months from the date of effectuation of the plan. In the event this option is not exercised, an assignable option, in the form of warrants, would revert to the reorganization committee for the purchase of 200,000 shares of class-B common at $30 a share, within 3 years from the effectuation of the plan. The reorganization committee would be authorized to transfer such option to any interests that it may select as being of the greatest advantage to the new company. The committee suggests the advisability of offering part of the option to the Chicago, Burlington & Quincy Railroad Company and the Chicago, Rock Island & Pacific Railway Company, because of the importance of these connections at Denver, and it is contended that there should be no objection to this association of interests on the part of the Missouri Pacific. Representatives

that the provision of section 77 (b) (5), permitting a sale at not less than a fair upset price, was designed for the identical purpose here in view.

The committee's plan, as well as the debtor's plan, is unacceptable to the trustee of the refunding and improvement mortgage, who undertakes to show that the rights of the bondholders are not adequately recognized under either plan. The trustee of the D. & R. G. first consolidated mortgage prefers the committee's plan but complains of the diversion of traffic and earnings to the cut-off route reflected in the results. The successor trustee under the R. G. Western first consolidated mortgage prefers the committee's plan but contends that the holders of bonds issued under this mortgage are entitled to better treatment than is offered under either plan. The Untermyer family group, owners of D. & R. G. first consolidated mortgage bonds, refunding and improvement mortgage bonds, general-mortgage bonds, and preferred stock of the Denver, contend that both plans are unfair to the present security holders in many respects and should be disregarded by us in formulating a new plan. The Security Research Bureau recommends several modifications in the committee's plan.

The trustee under the debtor's general mortgage prefers the committee's plan to the debtor's but on brief contended that the committee treated the general-mortgage bonds inequitably in relation to the unsecured creditors and the stockholders, and that a new class of second-preferred stock should be allocated to the general-mortgage bonds in place of the class-A common stock provided in the committee's plan. Later, in connection with its exceptions to the examiner's proposed report, the trustee suggested that the committee's plan be revised by eliminating the provisions for new common stock of classes A and B, and substituting a single class of no-par common stock, of which 750,000 shares would be issued in the reorganization. Of such stock, 408,618 shares would be issued to the holders of the general-mortgage bonds in satisfaction of their total claims for principal and interest ($44,587,800, including the interest from February 1, 1924, to February 1, 1929), 4,400 shares would be issued to the unsecured creditors, and 314,350 shares would be reserved for conversion of the new preferred stock. The 413,018 shares would be placed in escrow for a period not exceeding 5 years, and rights for the purchase of the stock at $100 a share would be issued to the debtor, or to the stockholders individually if an agreement could be reached between the two classes of present stock as to the proper allocation between them of such rights. The proceeds of sale would be distributed pro rata to the holders of the certificates of deposit, i. e., the present

holders of the general-mortgage bonds. This proposal is urged as a means of satisfying the claims of these bondholders before recognizing the stockholders, and at the same time avoiding a determination of the question of the equity represented by the stock. Apparently, if fully carried out, the plan would mean the payment by the proprietary companies of $41,301,800 in cash for control of the new company. It would further mean that the holders of the general-mortgage bonds would receive substantially the full amount of their claim in cash, while senior bondholders would be asked to accept various amounts of new securities, in some cases only income bonds and preferred stock. The largest single holder of the general-mortgage bonds is the Western Pacific Railroad Corporation, which is not represented in this proceeding.

In connection with the general-mortgage bonds, the trustee insists that any plan of reorganization should recognize the claim for interest, in the amount of $7,452,000, accrued between February 1, 1924, and February 1, 1929, in addition to the $7,327,800 of interest accrued between February 1, 1929, and June 30, 1938, the latter clearly being fixed interest under the provisions of section 4 of article 6 of the mortgage. The same section provides that the payment of interest accrued prior to February 1, 1929, shall not be mandatory even if earned, but if earned and available it shall be paid to the extent that, in the reasonable discretion of the board of directors, such payment is not inconsistent with due regard for the protection of the property and the maintenance of efficient service. Section 2 of article 8 provides that no dividends on any class of stock may be paid unless and until the full cumulative sinking-fund payments and the full cumulative interest on the general-mortgage bonds shall have been declared and paid, or set apart for payment.

In preparing its plan the debtor evidently considered the payment of interest prior to February 1, 1929, as discretionary and not a fixed charge. Counsel, on oral argument, offered no definite opinion on this point. The committee's plan does not include this interest as part of the obligation to the general-mortgage bondholders. Our view of the matter is that the claim of these bondholders is so large in relation to the indicated equity remaining for them, that as a practical matter it is immaterial whether the interest in dispute is included or not. For the purpose of the plan we shall therefore exclude this interest from the claim, without prejudice, however, to a judicial determination of the matter.

Because of the usual seasonal traffic fluctuations, the use of 6-month income periods for the determination of available net income, and the payment of interest and preferred-stock dividends

semiannually, as proposed by the committee, involves successive adjustments of bond interest and the use of interim dividends on the preferred stock in order that the aggregate payments to the security holders shall be based on the earnings of complete calendar years. This method, it is true, would result in a return to the security holders twice a year, earnings permitting, but it is desirable that the result of a full year's operation be ascertained before any contingent interest or dividends be paid (subject to the condition that the initial income period is six months), and that the entire amount of such interest and dividends earned be paid as soon after the close of the 1-year income period as is practicable. The date of the payment should be as stated below.

As has been shown, the debtor's proposal for a capital fund was that an annual payment of $350,000 be made from available net income after the payment of fixed charges, and that a second payment, representing the difference between $350,000 and 3 percent of total revenues, be made after the payment of interest on the proposed income bonds, if earned. The debtor's principal witness considered that 3 percent of total revenues would be a fair amount to be set aside for the capital fund, considering the amount of expenditures in the past and the possible difficulty of new financing at times in the future. As the committee views the matter, payments into the fund should be made semiannually in amounts up to 2½ percent of total revenues, subject to a maximum limit of $375,000, or $750,000 on an annual basis, the entire payment to follow directly the payment of fixed charges. We approve the latter provision on the ground that, if there is to be a mandatory capital fund; all payments thereto should precede the payment of contingent interest, and we further approve a limitation on the amount to be paid into the fund each year. The average gross charge to investment in road and equipment for the system lines during the 10-year period 1926–35 was $3,273,668 per annum, which is far in excess of 3 percent of the average annual gross revenues during that period. From the evidence it is difficult to predict the yearly capital requirements of the system after the present rehabilitation programs shall have been carried out, and obviously impossible to foretell future financing conditions. Following the debtor's plan, 3 percent of the average annual revenues during the 10-year period 1927–1936 would have been $848,203. On the basis of the estimate for a future normal year, 3 percent of the revenues would be $1,011,636. The principal witness for the Finance Corporation approved the committee's proposal for a maximum payment of $750,000, considering it sufficient.

Conclusions

The consolidation of the several companies for unified operation and management, which is an essential part of the plans that have been presented, is in accord with our findings in *Consolidation of Railroads*, 159 I. C. C. 522, wherein the Denver and the Salt Lake were grouped in system No. 18, Missouri Pacific. The Western Pacific was also included in that system, but the present record is inadequate for a determination of the question of merging the Western Pacific with the reorganized Denver. It justifies the conclusion, however, that the consolidation of the Denver, the Salt Lake Western, the Salt Lake, the Junction, and the Goshen Valley would be in the public interest, as unifying the Denver and its subsidiaries, eliminating unnecessary separate corporations, and effecting operating economies. Notwithstanding the fact that the Salt Lake, the Junction, and the Goshen Valley are not in trusteeship, and that none of the corporations has sought consolidation under section 5 (4) of the Interstate Commerce Act, as amended, we conclude that a consolidation of the aforesaid properties should be effected in connection with the plan. Any corporate action by the existing companies which may be necessary under the requirements of section 5 (4) of the Interstate Commerce Act, as amended, will be assured if and when our plan shall have been accepted in the manner provided in section 77 (e). As pledgee of the capital stock of the Salt Lake, the Salt Lake Western, and the Goshen Valley, the Finance Corporation is at present in a position of control with respect to the action of those corporations. The Governors of the States in which the several carriers operate were served, prior to the hearing, with copies of the plan of reorganization filed by the debtor, and advised of the provisions for consolidation contained therein.

The Public Service Commission of Utah, on its own behalf and on that of the Uintah Basin Railroad League, opposes the absorption of the Salt Lake in the new system on the ground that the independence of that carrier would facilitate the building of an extension westward from Craig through the Uintah Basin to Provo or Salt Lake City. These Utah interests likewise opposed the acquisition of control of the Salt Lake by the Denver. Such acquisition having been authorized by us and carried out, we think that this reorganization should not be hampered by the position taken by the Utah Commission. In view of the Denver's control of the Salt Lake, a consolidation of the roads will not alter the present situation in such a way as to prejudice the construction of a line through the Uintah Basin.

ard-gage lines west of Dotsero, $22,680,233; first and refunding mortgage 4-percent bonds, representing a first lien on all standard-gage lines east of Dotsero and a second lien on all other standard-gage property, $48,222,730;[1] general income mortgage 4-percent bonds cumulative for two years, representing a lien junior to that of the first and refunding bonds, $18,686,850; first preferred 4½-percent noncumulative stock, of $100 par value, $30,376,050; participating preferred 5-percent stock, of no-par value, 413,842 shares; common stock, of $1 par value, 200,000 shares; and a collateral note for $1,542,200 issued to the Chase National Bank. The bonds and stock proposed to be pledged as security for this note are not included in the foregoing totals.

The amount of first and refunding bonds stated includes $6,000,000 of bonds to be placed in the treasury of the new company to provide funds for 100 percent of the cost of additions and betterments and other corporate purposes during the first year after reorganization, of which bonds $3,000,000 would be available for immediate sale to the public and $3,000,000 would be available for sale to the Missouri Pacific and Western Pacific as required. Approximately $277,000 in cash would be paid to the holders of certain divisional bonds as an adjustment of interest rates. The debtor considers that the minimum amount needed for cash working capital is approximately $1,000,000. The provision for treasury bonds to be available for sale is considered by the debtor preferable to providing any specified amount of cash in the reorganization for working capital and additions and betterments.

The capital stock of the Utah Fuel Company would be pledged under the proposed general mortgage. As has been indicated, this stock is now under the first lien of the R. G. Western consolidated mortgage, subject to a right of redemption upon the payment of $6,000,000 in cash or upon the deposit with the mortgage trustee of $6,000,000, principal amount, of the consolidated-mortgage bonds. The company's balance sheet of December 31, 1936, shows the asset value of the fuel company property as $15,171,943, the par value of stock outstanding as $10,000,000, and the corporate surplus as $2,652,839. An appraisal of the property, made for the trustee of the R. G. Western consolidated mortgage by a mining expert, indicated a going-concern value of $4,653,720. As has been stated, the debtor, in applying its formula for allocation of earn-

[1] Not including additional future issues for (1) the purpose of refunding the $2,217,000 first-mortgage bonds of the Northwestern Terminal Railroad Company in the event that it is desired to utilize permanently the facilities of that company, (2) exchange for securities of the Western Pacific Railroad Company in the event of a consolidation with that company, and (3) refunding the Western Division bonds which may be issued.

ings by mortgage districts, credited this mortgage with an income of $83,333 per annum from the fuel company, based on dividends paid but not earned in the period 1932–34. In 1935 and 1936 small amounts of net income were reported. The property and its operations are completely described in the record. As part of the security for the R. G. Western consolidated-mortgage bonds, its value is an element in the claims of the trustee under that mortgage.

Including $1,805,000 of equipment obligations and $650,000 of trustees certificates, the total funded debt of the new company under the debtor's plan would be $92,937,013, the fixed interest charges $2,868,235, per annum, and the contingent interest charges $747,474 per annum. Dividend requirements on the first preferred stock would be $1,366,922 and on the participating preferred $2,069,210 per annum. The total capitalization of the new company, if a par value of $1 a share be assigned to the participating preferred stock, would be $123,926,905.

The theoretical application of income available for interest annually would be in the following sequence, under the debtor's program immediately upon consummation of the plan; (1) Fixed interest, $2,868,235; (2) fund for additions and betterments, $350,000; (3) fund for retiring first and refunding bonds (one-half of 1 percent per annum on the maximum principal amount at any previous time outstanding), $241,113; (4) contingent interest on income bonds, $747,474; (5) second payment to the fund for additions and betterments, 3 percent of gross revenues less $350,000; (6) fund for retiring income-mortgage bonds (one-fourth of 1 percent on the maximum principal amount at any previous time outstanding), $46,717; (7) dividends on the first preferred stock, $1,366,922; (8) dividends on the participating preferred stock, $2,069,210; grand total before dividends on the common stock, $7,939,671.

The foregoing figures omit provision for the payment of any undistributed-profits tax under the Revenue Act of 1936. The debtor submitted an estimate of the amount of such tax in the future, based on various amounts of net income available for interest, indicating $180,000 per annum as a probable maximum.

Expenditures for additions and betterments during three years after reorganization would be initially capitalized in full through the issue of not exceeding $6,000,000 of first and refunding mortgage bonds to be issued as treasury bonds. Thereafter, bonds might be issued under either the western-division mortgage or the first and refunding mortgage up to 75 percent of the cost of additions and betterments, the remaining 25 percent to be supplied through the proposed capital fund. The debtor's intention is that

the new first and refunding mortgage bonds shall constitute the principal medium, but not the only medium, of future financing.

As has been stated, the holders of unsecured claims, not coming under the six-months rule and not paid off currently, would receive new participating preferred stock at the rate of one share for each $100 of claims. This is with the proviso that, should any general creditors prove to have claims secured to such an extent as to justify better treatment, the debtor company, as reorganization manager, should be authorized to allocate other securities in settlement of such claims, subject to our approval. The debtor is of the view that the treatment of executory contracts, including the Northwestern Terminal Railroad Company lease, should be left to the new management and the court.

The plan is the result of a comprehensive study by the secretary-treasurer of the Missouri Pacific, and was made at the request of representatives of that company and the Western Pacific, acting as a managing committee of the Denver. Conferences on the development of the plan were held by its proponents with representatives of the Finance Corporation, the Chase National Bank, the Insurance Group Committee, and others. Resolutions approving the plan were enacted by the boards of directors of the several companies involved, except the Salt Lake and the Goshen Valley; but no action has been taken with respect to the application for authority to consolidate the properties in accordance with section 5 (4) of the Interstate Commerce Act, as amended. The debtor contends that under the provisions of section 77 (b) applications for authority to consolidate are unnecessary.

Disapproval of the debtor's plan was expressed by the Insurance Group, the Security Research Bureau, several mortgage trustees, the Railroad Credit Corporation, the Finance Corporation, and others. The Finance Corporation declined to give its consent, as pledgee of the stocks of the Salt Lake and the Goshen Valley, to the concurrence of these companies in the plan. It contends that during the period of the Denver's trusteeship no rental has been paid for the use of the Salt Lake Western line, nor have the trustees acted either to affirm or disaffirm the lease.

The chairman of the Finance Corporation is in favor of a consolidation of the Western Pacific and the Denver. A special committee of the latter's directors was appointed to negotiate such a consolidation, and in the event that it was undertaken the debtor was to file a supplemental plan. The debtor considers that the proposed western division mortgage might be extended to cover the Western Pacific property, and certain of the bonds reserved

under that mortgage could be issued to the holders of Western Pacific securities.

The Finance Corporation introduced evidence pertaining to the cut-off route, as compared with the route via Pueblo, for the purpose of showing the superiority of the former in respect of grades, curves, and other physical features, cost of moving freight and passengers, originated traffic, and many other matters. It contends that its loans to the Denver are fully secured, that it has extensive powers of control over the Salt Lake and the Salt Lake Western, and that it is entitled to such treatment in the reorganization as will fully satisfy its claims. Objection was made to the debtor's proposed offer of new bonds which would represent only a second lien on the western lines, and it was urged that all unpaid interest should be paid in full.

Insurance Group Plan

The Insurance Group committee represents seven mutual life-insurance companies which, taken together, owned $15,874,000 of bonds issued under the Denver's underlying mortgages, principally the R. G. Western and D. & R. G. first consolidated, but no bonds issued under the debtor's own mortgages. The holdings represent more than 10 percent of the principal amount of the bonds in each class outstanding. These insurance companies owned more than $91,000,000 of bonds and equipment obligations of the Missouri Pacific and its subsidiary companies, and nearly $15,000,000 of similar securities of the Western Pacific.

The formula used by the committee for the distribution of revenues and expenses is a modification of the debtor's formula, based on the same test period. Consolidation of the properties is likewise contemplated and, while consolidation with the Western Pacific is not directly provided for, the committee states that its plan leaves the way open for such consolidation.

The committee used the debtor's distribution of earnings by mortgage districts, as revised on the basis of actual waybills, adjusting the results thereof (1) by allowing 42 percent of the constructive-mileage adjustment for the cut-off, (2) by reallocating a certain group of equipment, and (3) by recognizing all fixed interest charges unpaid up to December 31, 1936. The net result of the changes was to increase the amounts of test-period earnings (totaling $3,926,223) assigned to the Junction first mortgage, the R. G. Western first-trust mortgage, and the D. & R. G. first consolidated mortgage, and to reduce the amounts assigned to other items, notably the lines subject to the lien of the Finance Corporation notes.

The arbitrary allowed to the cut-off in the committee's plan arises from an adjustment of the debtor's ascertainment of unit operating expenses for the two routes, respectively, such adjustment being confined to maintenance costs, which, it was thought, the debtor had not treated on a comparable basis. Rejecting the debtor's various reasons for the 175-mile arbitrary allowed to the cut-off, the committee asserts that if the cut-off were operated as a separate railroad no division of the through rate could reasonably be expected to exceed the 42-percent allowance.

The committee's adjustment with respect to the allocation of equipment results in a credit of $26,665 to the earnings of the D. & R. G. first consolidated mortgage district and a debit of like amount to the earnings of the refunding and improvement mortgage district. This amount represents the application of the 2-percent rental to equipment having a ledger value, less depreciation, of $1,263,265 as of December 31, 1936, and considered by the committee to be subject to the paramount lien of the D. & R. G. first consolidated mortgage rather than to that of the refunding and improvement mortgage. As to all other equipment the debtor's allocation of equipment under the several mortgages was adopted by the committee. This plan assigns the earnings of the Junction, in excess of the requirements of its present bonds, to the D. & R. G. first consolidated mortgage district, while the debtor assigns them to the refunding and improvement mortgage district.

In applying its formula, the committee arranged the present mortgages in four groups, viz, the R. G. Western district, the D. & R. G. district, the R. & I. district, and the R. E. & C. district, and based its computations on the total earnings allocated to each. In the case of the R. G. Western district, $16,415,667 of new first-mortgage fixed-interest bonds were to be issued for a like amount of claims of the present first-trust bonds, both actually outstanding and pledged, with all unpaid interest to December 31, 1936. This treatment recognizes the fact that the test-period earnings were in excess of the interest requirements of the first-trust bonds. For the total claims of the R. G. Western consolidated-mortgage bonds, the committee proposes to issue $8,938,577 of new first-mortgage bonds and $9,506,025 of new income bonds, the latter figure including $567,448 as an allowance for control of the Utah Fuel Company. The total amount of these new bonds is equal to the total amount of present consolidated-mortgage bonds, with interest. This result is arrived at despite the fact that the earnings in the test-period year, allocated to the consolidated-mortgage bonds, are shown as a deficit of $96,811. It further appears that, although the committee's calculations to determine the allowable

amount of fixed-interest and contingent-interest bonds purport to reflect average earnings during the period 1932–35, the test-period base has been adhered to in fact. In the brief filed by the Security Research Bureau many alleged errors in the calculations are pointed out.

The plan proposes a new first mortgage, secured by a lien on all the consolidated railroad properties, except the narrow-gage lines and their equipment, together with the stock of the Utah Fuel Company. Series-A bonds issued under this mortgage would be convertible into series B, would bear interest at 4 percent, and would mature in 15 years. The reorganization committee would have the power, subject to our approval, to reduce the term to not less than 10 years and to increase the rate of interest to not exceeding 4½ percent, in order that such bonds may be marketable at or near par. The series-B bonds would bear interest at 4 percent and have a term of 40 years. The first-mortgage bonds, which may be limited in amount by the terms of the mortgage, are to be issuable to the extent of 75 percent of the cost of additions and betterments. Income-mortgage bonds, subject only to the lien of the new first mortgage, would be issued under a mortgage closed at the amount of bonds to be issued in the reorganization. The income bonds would have a term of 50 years and an interest rate of 4½ percent, cumulative up to a maximum of 22½ percent. These bonds would be entitled to a sinking fund of one-fourth of 1 percent per annum on the total principal amount of bonds issued in the reorganization.

The plan proposes an issue of convertible preferred stock, entitled to dividends at the rate of 5 percent per annum, cumulative; common stock of two classes; and warrants carrying the right to purchase common stock. A new collateral note would be issued for the present bank debt, and provision is made for the issue of a promissory note to the Railroad Credit Corporation in the event the latter's note is not paid through distributions under the marshaling and distributing plan, or by cash. For the total amount of principal and interest due the Finance Corporation, approximately 58 percent is proposed to be paid in new first-mortgage bonds, series B, and 42 percent in new income bonds.

The chairman of the Finance Corporation advised counsel for the committee that if it is not found feasible to effect a consolidation of the Denver and the Western Pacific, and the plan of the committee is approved by us and affirmed by the court within a reasonable time, the Finance Corporation would finance, at par and accrued interest, $11,443,675 of new first-mortgage 4-percent

of the latter testified as to the established traffic relations between the Missouri Pacific and the Denver, and the possible unfavorable effect of a future alliance between the Denver and other systems, such as the Burlington.

The committee's proposed treatment of the stockholders of the Denver is predicated on a finding that the equity in the present stock is without a value and that the interests of present creditors must receive full consideration before those of the stockholders. However, the committee, recognizing the interdependence of the Denver, the Missouri Pacific, and the Western Pacific, and with a view to maintaining the through route which has been developed, has provided in its plan the above-described means whereby the proprietors may retain control of the Denver.

Cash proceeds received by the new company from the exercise of the warrants are to be used initially to redeem income-mortgage bonds issued to the Finance Corporation. The new class-A common stock would carry full voting power on all matters affecting the essential aspects of its proprietary interests, while the new class-B common stock, if and when one-half of such stock becomes outstanding, would be entitled to elect a majority of the board of directors of the new company, to consist of 12 members. One member would be elected by the holders of the income bonds, two by holders of the preferred stock, and two by the holders of the class-A common stock. The remaining members would be elected by the holders of the class-B common stock.

All the common stock would be issued to the reorganization committee as voting trustees, to be held by them for a period not exceeding 3 years, but the voting trust may be terminated within 90 days from the date of payment for the warrants issuable to the reorganization committee. The reorganization committee would consist of seven members, of whom six would represent a like number of classes of present bonds, and one would be designated by the Finance Corporation.

The plan provides that it shall not be carried out until it shall have been accepted by or on behalf of the holders of at least two-thirds in principal amount of each class of the outstanding bonds of the debtor and by the Finance Corporation, nor unless either (1) the plan shall have been accepted by creditors, other than bondholders and the Finance Corporation, holding at least two-thirds in principal amount of the claims of each class and by the stockholders of each class holding at least two-thirds of the stock of such classes, or (2) provision shall have been made for protecting the interests of such nonassenting classes of creditors and

stockholders as provided in article VIII of the plan, provided that the reorganization committee may under certain conditions eliminate the requirement for consent as to any class of bondholders or the Finance Corporation upon substituting therefor the provision for protecting the interests of the bondholders and the Finance Corporation as is provided in article VIII as to the other classes.

Article VIII of the plan provides for a sale of the debtor's property under certain circumstances in the following manner. If the holders of more than one-third in principal amount of any class of creditors (other than the holders of bonds or the Finance Corporation, except to the extent that the above requirement for a two-thirds consent by the holders of any such class of bonds or the Finance Corporation may have been eliminated by the reorganization committee) of the Denver, the Salt Lake Western, and the Junction, as they have been or may be classified by the court, or the holders of more than one-third of the shares of the Denver's stock of any class, shall not have accepted the plan within such period as the reorganization committee, with the approval of the Commission and the court, may determine, after holders of at least two-thirds in principal amount of each class of bonds affected by the plan and on the part of which two-thirds consent shall be required by the plan as now existing or hereafter modified, shall have accepted the plan, the property of the Denver shall be sold at public auction at not less than a fair upset price as determined by the court, and the nonassenting creditors of such class and/or the nonassenting stockholders of such class, shall be entitled to receive their aliquot proportion of the proceeds of such sale, after deducting therefrom all expenses of such sale and the amount which would be required to pay in full, of principal and unpaid interest accrued to the date of such sale, all creditors whose claims are prior in lien or superior in equity to the claims of such nonassenting creditors or the rights of such nonassenting stockholders. Upon any such sale the property may be purchased for the benefit of the new company by the reorganization committee, and in that event there shall be applied on account of the purchase price therefor the distributive share of the proceeds of sale of all securities the holders of which shall have assented to the plan and the securities, though not assenting to the plan, of all classes of which two-thirds or more in amount have assented to the plan.

This provision was incorporated because of doubt whether the confirmation of the plan, without acceptance by two-thirds in amount of each class of creditors and stockholders, would be within the scope of the bankruptcy power or would be permissible under the due process clause of the Constitution. Counsel assert

New capital structure.—As hereinafter used, the term "new company" will be understood to mean either the reorganized debtor or a new company created to take over the properties and assets of the several existing companies.

The effective date of the plan should be June 30, 1938. The obligations and capital stock of the Denver and the affiliated companies outstanding on that date, excluding intercompany holdings and securities under pledge, are listed in the appendix to this report. The total amount of debt shown, $171,374,879, is approximately $14,318,000 in excess of that outstanding on December 31, 1936, the date when the filed plans were to become effective, and such increased obligations must be provided for. Under the provisions of section 77 (d) we may, after public hearing, approve a plan which may be different from any which has been presented and will, in our opinion, meet with the requirements of subsections (b) and (c) and be compatible with the public interest.

The capital structure of the new company which we approve as meeting the requirements of the act, and the allocation of new securities to the holders of certain classes of claims, are shown in tabulated form in the appendix which also shows the principal amounts of securities, excluding those which may be issued for pledge, and the annual charges thereon.*

The record contains data showing the earnings of the system lines between 1927 and 1936, inclusive, and various analyses made from these data, as already described. Among the significant facts are the average annual income available for interest in 1934–36, after intercompany eliminations, amounting to $3,118,197 a year, that of the constructive 12-month period used by the debtor, amounting to $3,926,223, and the 1932–35 average of $3,606,920 a year, to which the committee applied a coverage factor of 1.3 and arrived at $2,774,554 as the allowable amount of new fixed interest charges. This was considered by the committee a reasonable measure of the probable low range of future earnings. Reference was made to indications that the revenues of 1937 would exceed those of 1936 and that the trend would continue upward. The testimony may have tended to support such a view, but the facts as later reported to us are that the combined income of the Denver and the Salt Lake available for interest approximated $296,000 in 1937 and $673,000 in 1938. The Denver's own operation resulted in a deficit of $186,290 in 1937 and an available income of $223,356 in 1938. The plan recommended by the examiner was predicated on the record up to the close of 1936. But the sub-

* Appendix is omitted in this printing.

sequent decline in earnings, even though common to many roads in the same period, cannot be entirely ignored in a consideration of the question of new fixed charges. Neither should the reorganization proceeding be subjected to undue delay pending a demonstration that the carriers can again earn more than $3,000,000 a year. As we regard the situation, the initial issue of new first-mortgage bonds should be restricted to the minimum financing requirements of the reorganization. Subject to adjustment for conditions which cannot be determined until later, the amount of new first-mortgage 4-percent bonds contemplated under our plan and apparently necessary as shown in the following discussion, is $29,403,144, and the fixed interest charges on such bonds, the equipment-trust certificates, and the indebtedness to the Chase National Bank and the Railroad Credit Corporation, will amount to approximately $1,348,536 per annum. This sum exceeds the average income of $1,128,869 available during the 3-year period 1936–38, the period of lowest system earnings during the last decade, and in our opinion should not be increased. Studies have been made to ascertain the effect of deferred maintenance on the property in previous years which was in part made up by the expenditures for maintenance in 1936–38. While necessarily giving approximate results, these studies indicate that the average system income available for interest during the 3-year period, as adjusted, was about $2,893,255. Under the plan herein approved the fixed interest requirements, plus the maximum payment into the capital fund, would amount to $2,098,536, subject to some possible increase in the amount of first-mortgage bonds issued in the reorganization, as has been indicated. Thus, on the basis of the adjustments shown, the earnings of the 3-year period 1936–38 would provide a coverage of 1.38 for those charges. In giving this consideration to the low earnings in recent years our position is not that the system lines will never regain their former earning power, or exceed it, but rather that, with the present conditions in the railroad field and in the public interest, a conservative policy should be followed in deciding what level of income to take as the reasonably assured earning power of the system, as such level affects the amount of fixed interest charges to be permitted in the future. We find that, after due consideration of the probable prospective earnings of the properties in the light of their earnings experience and other relevant facts, there will be adequate coverage of these fixed charges of the new company by the probable earnings for the payment thereof.

The above stated amount of new first-mortgage bonds represents the aggregate amount of the debt to the Finance Corporation, the sum necessary to redeem the Salt Lake bonds outstanding, the prin-

cipal amount of the Denver's trustees' certificates outstanding, and $1,000,000 to cover reorganization expenses, etc. If the financing necessary in connection with the last three items should entail a larger amount of bonds for pledging purposes, the stated total would be correspondingly increased, but the total actual debt upon which interest would be payable would not be increased unless it was found necessary to sell the bonds at less than par. Provision is also made in the plan for the possible issue of first-mortgage bonds for the purpose of refunding the existing bonds of the Northwestern Terminal Railroad Company if that should be found desirable.

The total debt of the new company under this plan would approximate $76,232,510, and the total capitalization $147,433,354, taking the no-par common stock at $100 a share. The total maximum annual charges ahead of the common stock would be approximately $5,758,639 per annum.

The basis for the limitation of annual fixed interest charges and capital-fund payment to about $2,098,536 has been stated. The total debt, including income bonds, should not only bear a proper relation to total capitalization but should be such as to render the payment of dividends probable, at least on the new preferred stock, under normal conditions of business, as far as such conditions can be estimated from the facts of record. This requirement is in justice to the bondholders who are to receive preferred stock in part settlement of their claims, and, is, moreover, desirable in order to promote the use of preferred stock as a means of financing. The total charges ahead of dividends on the preferred stock, under the plan herein approved, will be slightly in excess of $4,000,000, and the full dividend requirements on that stock will be about $1,665,000 a year. The $4,000,000 figure reflects an initial issue of approximately $42,000,000 of 4½-percent income-mortgage bonds, allocated as shown in the appendix. That such total charges, and the amount of new bonds to which they correspond, cannot be increased without serious detriment to the prospective value of the new preferred stock is plain from the carriers' earnings record. In no year since 1931 has the total income available for interest reached $4,000,000. The average available income for the years 1932 to 1935, inclusive, used as a basis by the committee, was $3,606,920. Practically the same amount is reached by averaging the nine years 1930 to 1938, inclusive, which include the high of $8,060,528 in 1930 and the low of $295,504 in 1938. The adjustments tentatively made in our studies for undermaintenance and overmaintenance, would reduce the average somewhat. The debtor's carefully prepared forecast for a future normal year is

not overlooked in this connection, but the trend of earnings since it was presented discourages reliance on the results of such a study. Even should these results be realized, the earnings on the new common stock would amount to only $1.20 a share.

As hereinbefore stated, the report of our Bureau of Valuation shows the cost of reproduction of the system properties, less depreciation, plus lands and rights, working capital, and net additions and betterments to December 31, 1936, as $147,717,268. In the light of all the evidence it is clear to us that the approved amounts of fixed-interest bonds, of total debt, including income bonds, and of preferred stock are the maximum amounts which should be allowed in the formulation of a sound plan.

The following provisions for the new bonds and stock; capital fund, sinking fund, means of future financing, etc., are based upon those incorporated in the committee's plan, with modifications where we disapprove the committee's suggestions or where those suggestions are inconsistent with the new capital structure. Such modifications consist chiefly of lengthening the term of both issues of bonds, making the income mortgage an open mortgage, placing the income periods and the payment of bond interest on an annual basis instead of a semiannual basis, changing the terms of the capital fund so as to make accumulations of unappropriated sums available for additions and betterments as well as interest on the first-mortgage bonds, making the new common stock of one class only, altering the function of the voting trust, and eliminating the provision for warrants, and modifying the restrictions on future issues of stock so as to facilitate the use of stock in future financing. With respect to any matters of detail not provided for herein it is to be understood that the reorganization committee, with the approval of the court, may determine the proper terms, provided that such terms shall conform to the plan herein approved.

Note—"(Here follows a description of the terms and conditions of the securities to be issued by the new company, together with provisions as to the order of application of available net income. Since these relate to a plan which was not approved, the subject matter is omitted here and reference is made to the description of new securities in the approved plan and the application of available net income in the order of June 14, 1943.)"

Formula, matters in dispute.—The major questions in this case in connection with the application of a formula for establishing the relative earnings of the several mortgage districts are (1) the period to be used as a basis; (2) the mileage to be assigned to the cut-off; (3) the treatment of the excess earnings of the Junction line; (4) the liens of the mortgages with respect to certain units

of equipment and the percent of value to be allowed for use of equipment; (5) the treatment of branch lines subject to the first lien of the refunding and improvement mortgage; and (6) the disposition to be made of the stock of the Utah Fuel Company. Also entering into the computations were the adjustment of revenues on the narrow-gage lines because of the fact that the average freight revenue per net ton-mile on those lines is approximately 1.45 times that on the standard-gage lines, an adjustment of the revenues of the D. & R. G. consolidated mortgage district because of the failure of the potato crop in the San Luis Valley in 1934–35, an allowance to the R. G. Western consolidated mortgage district for the assumed earnings of the Utah Fuel Company, and an allowance to the D. & R. G. consolidated mortgage district for the use of the shops at South Denver also used for repairs on equipment operating over other divisions of the system. More important matters as to which the parties are in disagreement involve the rights of the bondholders and other secured creditors to the payment of interest accrued from the date of filing the petition under section 77, the question of a special provision for the holders of bonds secured by mortgages on the western divisions of the Denver, the claims of the Finance Corporation, the equity of the debtor's present stockholders, and the future control of the new company. On all these matters the testimony, briefs, and oral arguments are exhaustive. It is impossible in this report to recite in detail the claims and contentions made by all the parties.

Certain interveners objected to the use of the test-period year ended June 30, 1935, as a measure of the earning power of the several divisions of the system on the ground that the debtor's adjustments of the actual revenues and expenses resulted in a constructive figure which, in any event, does not fairly represent the full effect of the establishment of the cut-off route. We are unable to see how such effect could reasonably have been ascertained. All the adjustments of the actual operating results were fully explained. The committee accepted the result as a basis for its formula, and most of the parties offered no objection to it. The study, in fact, represents 18 months of operations after the opening of the cut-off. Clearly the operating results in 1936, 1937, or 1938, when earnings were greatly reduced, would not afford a representative basis, assuming it practicable to employ these results in a new formula computation. We are of the opinion that great precision cannot be expected in such a matter and that the test-period basis of income available for interest, as adopted, is a reasonable basis for the distribution of earnings and the development of a plan.

The cut-off.—In its first analysis the debtor showed the income of the cut-off available for the payment of interest in the test period as $85,241. This amount, plus the earnings on the bonds, etc., pledged with the Finance Corporation being insufficient to cover the interest charges on the new bonds assigned to the Finance Corporation, the shortage was supplied from the earnings of two of the western mortgage districts. The second analysis, on the waybill basis, showed the earnings of the cut-off to be $370,246, and this is the result finally adopted by the debtor. Both the first and second analyses represent the allowance of 175 additional miles to the cut-off. The third computation was on a straight mileage basis and showed a deficit of $285,993 for the cut-off. The committee added to the net of the cut-off, on a straight mileage-prorate basis, 42 percent of the increase in net earnings which it would have under the 175-mile arbitrary, computed on the waybill basis. The test-period revenues involved with the cut-off consist of approximately $2,100,000 from overhead traffic and $1,340,000 from local traffic, the latter originating or terminating at points on the Denver. The overhead traffic formerly moved about 400 miles on lines west of Dotsero and 342 miles east from Dotsero to Denver, via Pueblo. The cut-off shortens the distance between Dotsero and Denver to about 167 miles. In dividing the test-period revenue from overhead traffic between the cut-off and the mortgage districts west of Dotsero on a mileage basis, the latter would obviously receive a large increase if the shortened length of haul east of Dotsero were used. The debtor believed that, since the western districts benefit by all new traffic that is attracted to the cut-off route, they are not entitled to the additional earnings computed on the basis of the actual mileage of the cut-off. The debtor also considered that, because of the large investment in the cut-off, that line is entitled to credit for all the revenue which formerly accrued to the old line via Pueblo. Other reasons given for allowing the 175-mile arbitrary include the alleged higher operating cost over the cut-off as compared with the Pueblo route, high maintenance costs on the cut-off and the undeveloped condition of that route during the test period, the rental of the Moffat Tunnel, the saving in mileage, and the desirability of having the earnings represented by the collateral held by the Finance Corporation support the proposed allocation of first-mortgage bonds to that creditor.

Despite the admitted detrimental effect of the diversion of traffic to the cut-off on the earnings of the old line east of Dotsero, and the validity of some of the objections raised to the theory followed by the debtor, e. g., increasing operating costs west of Dotsero due to meeting schedules on both routes, we are persuaded that

the use of the constructive mileage of the cut-off is justified on the ground alone that a lesser mileage would distort the earnings of the western mortgages. It is not clear how the D. & R. G. consolidated mortgage can be compensated for the construction of the other route to Denver, which tends to render the Pueblo route obsolete, without unduly expanding the new capital structure. The debtor takes the view that the private interest of the consolidated mortgage is subordinate to the public interest in the shortening of the haul. Some of the through traffic moving over the cut-off is new traffic which probably would not have come to the Denver if only the Pueblo route were available. The system as a whole should benefit ultimately from the cut-off operation, the economies from consolidating the several properties, and the saving in interest on the Salt Lake bonds.

Junction earnings.—The formula studies show the gross revenues of the Junction in the test period as $1,247,564, allowing for the 175-mile arbitrary for the cut-off, and as $1,396,826 on the basis of the straight mileage prorate. Under the committee's formula, allowing 42 percent of the 175-mile arbitrary, the net income of the Junction available for interest was $275,663.

The lease of the Junction property provided that 30 percent of the Junction's gross revenues be paid as rental but that the payment should in no event be less than the amount of the annual interest on the first-mortgage bonds, or $100,000 per annum. All the capital stock of the Junction being pledged under the refunding and improvement mortgage, the trustee under that mortgage argues that this mortgage is entitled to be credited with all the net earnings of the Junction after payment of interest on the bonds, up to 30 percent of its gross revenues. The trustee further contends that an agreement made by the boards of directors of the Junction and the Denver in 1925, which modified the lease by limiting the rental to $100,000 a year, is void. The debtor adopted this theory, crediting the net income of the Junction to the refunding and improvement mortgage.

The trustee of the D. & R. G. consolidated mortgage, as well as the Insurance Group committee, claims that the earnings of the Junction should be allocated to the consolidated-mortgage bonds because the after-acquired-property clauses in the consolidated mortgage cover the leasehold estate in the Junction property vested in the principal debtor as the result of an agreement dated December 24, 1889. This agreement provided for the making of a formal lease covering the same subject matter as the agreement. No formal lease was subsequently made. However, there seems to be no reasonable doubt, considering all the terms of the agreement, and

the fact that the Denver has had some 47 years of occupancy under the agreement, that the effect of the agreement was to vest a leasehold estate in the principal debtor. See *Levin* v. *Saroff*, 201 Pac. 961 (Cal. App.); *People* v. *Saint Nicholas Bank*, 3 N. Y. App. Div. 544 (affirmed 151 N. Y. 592). Under Colorado law, a lease of land is regarded as real property. *Bonfils* v. *McDonald*, 270 Pac. 650.

The D. & R. G. consolidated mortgage, dated July 15, 1886, conveyed to the trustee—

> All the property real, personal, and mixed * * * of every kind and description, now owned or hereafter to be acquired, including its entire line of railroad now owned or hereafter constructed" * * * "together with all the estate, right, title, interest, property * * * as well at law as in equity, present and future * * *.

The mortgagor agrees to make—

> all such further acts, deeds, conveyances, * * * for the better carrying out the purposes hereof, and assuring unto the said Trustee * * * in the trust hereby created, upon the trusts and further purposes herein expressed or intended, all and singular the lands, * * * property, railways, * * * lease holds * * * now owned * * * or subsequently to be acquired, * * * and all other property and things whatsoever, which may be hereafter acquired, in aid of or by way of substitute for, or for use for the purposes of the same * * *.

It may safely be concluded therefore that the leasehold estate in the Junction property became subject to the lien of the D. & R. G. consolidated mortgage. This lien is secondary to the Junction first mortgage dated December 1, 1889, but because prior in time it is prior to the mortgage created by the Junction on January 1, 1929, which, together with the stock of the Junction, is pledged under the refunding and improvement mortgage.

The situation as to the Junction stock is substantially this: One of the predecessors of the principal debtor, having acquired in 1889 a leasehold of the Junction property, pledged it as of July 15, 1886, under the D. & R. G. consolidated mortgage of that date. Many years later, in 1924 or thereabouts, the debtor, being the owner of the stock of the company (the Junction) which had conveyed the leasehold estate, pledged that stock as additional security for the refunding and improvement mortgage. The trustee of that mortgage points out that subsequent to the creation of the mortgage the debtor, through its ownership of the capital stock of the Junction, caused the lease to be modified by (1) decreasing the rental from 30 percent of the gross revenue, with a minimum sufficient to pay the interest on the $2,000,000 of the Junction bonds, and (2) transferring the obligation to pay for additions, betterments, and improvements from the debtor to the Junction. Through the

latter arrangement the Denver was able to use funds obtained from the sale of refunding and improvement bonds for the additions, betterments, and improvements on the Junction, and to have the Junction issue its bonds for that amount ($906,000), which bonds were then pledged under the refunding and improvement mortgage. The trustee of that mortgage argues that these transactions rendered the Junction securities pledged under the mortgage practically worthless, that the transactions were void as being in violation of the purposes and spirit of the refunding and improvement mortgage, and that full effect must therefore be given to the lease in its original form. In our opinion, there is no merit in these contentions. The refunding and improvement mortgage authorized the debtor, without the consent of the trustee—

> from time to time to change, amend, * * * in whole or in part, any leases whose terms do not extend beyond the latest date of maturity of the refunding bonds at the time outstanding, or any leases whatever their term to or with a lessor which, at the time, is a controlled company of the railroad company, or any trackage rights, or any contracts relating to the mortgage premises.

That mortgage also permitted reimbursement out of the proceeds of the refunding and improvement bonds for additions, betterments, or improvements or real property owned by a corporation 90 percent or more of the capital stock of which was pledged thereunder, provided that bonds of such corporation, in principal amount at least equal to the amount of such expenditures, were pledged under the refunding and improvement mortgage. The mortgage also authorized the debtor to vote pledged stock for all purposes not inconsistent with the provisions or purposes of the mortgage.

We conclude that any earnings of the Junction during the test period in excess of the interest on its first-mortgage bonds should be credited to the D. & R. G. consolidated mortgage.

Equipment.—The chief controversy with respect to equipment involved the question whether certain equipment, having a depreciated value of $1,263,265,[5] as of December 31, 1936, is subject to the lien of the D. & R. G. consolidated mortgage or to that of the debtor's refunding and improvement mortgage. The trustee of the latter mortgage, in view of the complex problems of fact and law involved in a judicial determination of the matter, has accepted the committee's allocation of this equipment to the lien of the D. & R. G. consolidated mortgage, and no definite objection to such allocation has been presented by the other parties. Without attempting to decide this question on legal grounds, we think the

[5] As stated by the trustee of the refunding and improvement mortgage. The amount used by the committee was $1,333,252, as of December 31, 1935.

plan may properly give effect to the committee's allocation as a compromise reached by the principal interest affected. On such basis the depreciated book value of the equipment subject to the direct first lien of the refunding and improvement mortgage as of December 31, 1936, was $6,005,357, and that of the equipment subject to the first lien of $1,805,000 of equipment-trust obligations, was $6,575,955. The aggregate depreciated value of the standard-gage equipment covered by these liens was $11,408,021. Such equipment constituting nearly two-thirds of all standard-gage equipment on the debtor's system, the refunding and improvement mortgage trustee contends that, if such equipment is to be placed under the lien of a new first mortgage, the holders of refunding and improvement mortgage bonds should receive appropriate amounts of the new first-mortgage bonds. Approximately 70 percent of the refunding and improvement mortgage equipment is used on the R. G. Western and Junction lines.

The second matter in dispute is the adoption by the debtor in its formula, and by the committee in its plan, of a rate of 2 percent per annum applied to the estimated depreciated value of equipment used on each mortgage district. On this basis the committee computed the test-period earnings of the refunding and improvement mortgage equipment at about $118,000. In support of the 2-percent rate the debtor stated that the return on its investment in road and equipment during the test period was about 1.25 percent, and that, giving effect to the extra value of equipment because of its mobile nature, and the fact that the equipment was taken at depreciated value, a rate of 2 percent was considered fair. This conclusion is defended by counsel for the committee who argue that the equipment is not in fact available for movement generally but is part of the corpus of the estate and is entitled to earn only what the estate can earn. Moreover, counsel contend that the depreciated book value used is much too high, in that the element of obsolescence has not been considered. The trustee of the refunding and improvement mortgage presented an exhaustive analysis which among other things included computations of earnings on investment, based on adjusted income figures, and the cost of reproduction of the properties, less depreciation, plus the value of lands and rights. These computations showed earnings ratios of 2.94 percent and 2.79 percent for the test period based on the elements of value of the property, as reported by the Bureau of Valuation, with certain adjustments. The record contains a statement of 28 issues of equipment-trust certificates in 1936 by various railroad companies, the average interest rate being slightly in excess of 3 percent. The trustee shows that the average rate on the debtor's equipment-trust

obligations was about 5 percent. It calculates the average return in the test period on the mortgage divisions which use the refunding and improvement mortgage equipment at 4.514 percent, this being a weighted average representing the proportionate use of such equipment by these divisions. The trustee further refers to the reports of division 4 in *New York, N. H. & H. R. Co. Reorganization*, 224 I. C. C. 725, and *Chicago, I. & L. Ry. Co. Reorganization*, 228 I. C. C. 209, in which division 4 approved rates of return on equipment equal to the prevailing rates on the carriers' equipment-trust certificates, viz, 4½ percent and 5 percent, respectively. As indicated in the New Haven report, a rate between 4 percent and 6 percent is in accordance with established practice between railroads. In the present case we are of the opinion that for the purposes of this plan an increase of the 2-percent rate used in the formulas to a rate of 4 percent, which the trustee indicates will be acceptable to it, is fully justified.

Branch lines.—The financial result of operating the branch lines subject to the first lien of the refunding and improvement mortgage affects the ascertainment of the earnings of that mortgage district. The standard-gage branches are 13 in number, totaling about 86 miles, including the Pacific mine and Hooper-Cox branches, not in operation in the test period. The operating loss from these lines, as calculated by the debtor and the committee, was approximately $40,000 during the test period. On account of such ascertainment of loss, the amount of first-mortgage and income-mortgage bonds issuable to the holders of the refunding and improvement mortgage bonds was reduced about $870,000 by the debtor and about $1,000,000 by the committee. The system revenue contributed by these branches approximated $1,500,000, which, according to the mortgage trustee, yielded approximately $1,000,000 of net revenue.

The trustee under the mortgage attacks the debtor's and the committee's estimates of loss on the branches principally on the ground that an unduly small proportion of the revenues was credited, and an unduly large proportion of the system taxes were charged. The trustee undertook to show that, by giving the branches a 15-percent division of the revenues and by adjusting operating expenses and taxes, the net earnings of the branches would be about $100,000. The data used were admittedly incomplete, and the methods followed were shown to be questionable by counsel for the committee. Such earnings from the branches cannot be considered as established, but on the other hand, in view of the large amount of system revenue derived from the traffic orig-

inating or terminating at stations on the branches, the propriety of charging them with a substantial loss may be doubted. We consider it fair under the circumstances to disregard the alleged loss on the branches in dealing with the refunding and improvement mortgage bonds.

Utah Fuel Company.—Reference has been made to the data of record in connection with the value of the Utah Fuel Company stock. The pledging of the 100,000 shares of this stock with the trustee of the R. G. Western consolidated mortgage was described in the report of division 4 in *Denver & R. G. W. R. Co. Reorganization*, 82 I. C. C. 745, 753, and in the report of the Commission in the same proceeding, 90 I. C. C. 141, 148. The title to the stock is vested in the Missouri Pacific and Western Pacific, which by an agreement dated December 20, 1924, provided for a voting trustee and the payment of any dividends to the debtor so long as any accumulated dividends on the debtor's preferred stock remain unpaid.

In allocating earnings to the mortgage districts the debtor credited the R. G. Western consolidated mortgage with $83,333 from the fuel company's stock, by arbitrarily spreading a $250,000 dividend, which was declared out of capital in 1933, over three years, and the debtor's principal witness considered that treatment as adequate to absorb the whole value of the fuel company's stock. The committee allowed the R. G. Western consolidateds $567,448 of new income bonds, based on the earnings and so-called control value of the fuel company.

The trustee of the mortgage objected strongly to these appraisals, citing the report made by the mining expert. He filed exceptions to the examiner's proposed report, with respect both to the new securities assigned therein to the R. G. Western consolidated bonds and to the proposed provision that the Utah Fuel Company stock be pledged under the mortgage securing the new income bonds. The trustee suggests that the stock and its dividends be pledged as additional security for a special issue of new income bonds and that all of such bonds be assigned to the R. G. Western consolidateds.

Counsel for the debtor suggest that the parties agree to a distribution of the fuel company's stock among the holders of the R. G. Western consolidated-mortgage bonds on terms that might be found reasonable. Such a distribution seems to us fair in principle, especially in view of the provision of our plan whereby these bondholders will receive no new bonds and the fact that both the

debtor's and the committee's plans gave these bondholders the benefit of the fuel company's earning power, as they estimated it. In our view, the plan approved by us should provide that the trustee under the mortgage securing the R. G. Western consolidateds be permitted to obtain the release of the equities of redemption in the stock, and distribute the stock among the holders of bonds in any manner acceptable to them, or to enforce its rights as pledgee of the stock, the mortgage being in default, the proceeds recovered to be distributed to the holders of the bonds.

Accrued interest.—The debtor's plan recognizes accruals of interest on secured debt only to the extent that it was earned subsequent to the date of filing the petition under section 77, thereby eliminating about $4,770,000 of interest accrued to December 31, 1936. Even as to the portion of the interest that was earned, the debtor offered securities junior in rank to those allocated to the principal obligation. Counsel contend that interest after the basic date, i. e., the filing of the petition, is not allowable unless the estate is found to be solvent and an equity in the stock exists; that all claims must be dealt with as of the basic date; that a continued accrual of interest should not be allowed to wipe out a debtor's equity or to distort the relationship of claims. This is part of the debtor's general argument in connection with the equity of the present stockholders and the applicability of the composition principle in reorganization cases.

The debtor's mortgages provide that principal and interest are equally secured by the lien, and it seems evident that any interest accrued at the prescribed rates and remaining unpaid is as much a part of the debt as the principal. We are unable to agree with the debtor's view that the secured claims must be dealt with as of the date of the filing of the petition. *Spokane International Ry. Co. Reorganization*, 228 I. C. C. 387, 233 I. C. C. 157, *Wickwire Spencer Steel Co.*, 12 Fed. Supp. 528, and *Ticonic National Bank* v. *Sprague*, 303 U. S. 406.

Mortgages on the western lines.—Because of the showing that the earnings of the Denver's western lines during the test-period year were more than adequate to cover interest charges on the bonds representing first liens on such lines, the debtor proposes that the Junction first 5's and the R. G. Western first-trust 4's be exchanged, in each case, for like principal amounts of new 3½-percent bonds issued under a mortgage secured by a first lien on the Junction property, the R. G. Western property, and the Denver's property lying between Dotsero and Rifle, and between Grand Junction and Crevasse, Colo., thus placing all lines west of Dotsero

under the direct lien of the new western-division mortgage. An additional amount of new 3½-percent bonds, or a corresponding payment in cash, is offered to compensate the bondholders for the loss of interest to maturity on the present Junction bonds and R. G. Western bonds. Such maturities are December 1, 1939, and July 1, 1939, respectively. It is contended by counsel for the debtor that the holders of the bonds in question should get all that they could receive in a liquidation or foreclosure. The relatively high earning power of these lines, even on the basis of the cut-off mileage used in the committee's formula, is uncontroverted.

The committee considers that "nothing can duly recognize the position of these bonds short of a new first-lien bond for the total of their principal and accrued unpaid interest, the new bonds to be of such interest rate, maturity, and terms as to sell at par." In order to meet this requirement, as has already been stated, the committee proposes the issue of new series-A bonds having a relatively short term, a permissible interest rate up to 4½ percent per annum, and other features intended to assure the required market value.

The Finance Corporation disapproved the creation of a separate western-division mortgage, because the new first and refunding mortgage bonds, which the debtor proposed to offer the corporation in settlement of its claim, would constitute only a second lien on the profitable western lines. The provision made for the western bonds by the committee was in the belief that a separate mortgage is unnecessary. The committee's proposal was apparently more acceptable than the debtor's to the trustee of the R. G. Western first mortgage and the Junction first mortgage, but the examiner's recommended plan, assigning new first-mortgage bonds, without special terms as to interest rate and maturity, was vigorously rejected by the trustee. Counsel for the committee concur in the position taken by the trustee, which is that any plan which does not recognize the preferred status of the western first-lien mortgages in the matter of earning power, and which does not give them preferred treatment, is inequitable, unfair, and would deprive the bondholders of their property without due process of law.

The advantages of new mortgages on the entire property of the system seems to us important from the standpoint of simplicity in the capital structure, from that of future financing, and as conducive to the cooperation of the Finance Corporation in effecting a consolidation of the lines and in general in carrying out the plan. The relative earnings position of the R. G. Western first-trust bonds and the Junction first-mortgage bonds may be recognized in

the allotment of new securities without the use of a separate mortgage. Under the capitalization which we consider permissible, however, it is impossible to assign new first-mortgage bonds to these claims or to those of any of the debtor's bondholders. The holders of the bonds in question will receive new income-mortgage bonds in amounts equal to the total claim for principal and interest as of the effective date of the plan, and the holders of bonds secured by mortgages on other parts of the debtor's lines will receive lesser amounts of new bonds in accordance with the indicated earning power of the respective lines, as will be explained later. Proportional sacrifices on the part of the first-lien bondholders are essential to the consummation of a plan at this time. It is not a matter of successive liens on the same physical property but more in the nature of parallel liens, the treatment of which depends primarily on relative earnings.

Finance Corporation claims.—The obligation of the debtor and secondary debtor to the Finance Corporation, in total amount of $11,959,469, as of June 30, 1938, is secured by pledge of numerous securities, hereinbefore described, among which are the capital stocks of the Salt Lake, the Salt Lake Western, and the motor companies, $4,385,000 of the Denver's refunding and improvement mortgage bonds, $1,395,000 of the R. G. Western consolidated-mortgage bonds, and $1,266,000 of the Salt Lake income bonds. The Finance Corporation introduced a large amount of evidence to show that its claim is entitled to settlement in cash or in readily marketable securities, particularly in view of the independent earning power and value of the Salt Lake.

The treatment accorded the Finance Corporation in both the debtor's plan and the Insurance Group plan recognized the Finance Corporation claims as fully secured. These parties and others, however, filed exceptions to the examiner's proposed report, recommending the allotment of new first-mortgage bonds for the full amount of the claim, on the ground that such treatment was inconsistent with that recommended for the several classes of securities pledged to secure the loans, and that the proposed allocation of new first-mortgage bonds to the Finance Corporation was unduly liberal, resulting in an injustice to the present bondholders, particularly the holders of the R. G. Western consolidateds and the D. & R. G. consolidateds. The complaint arises more from the fact that the examiner reduced the aggregate amount of first-mortgage bonds from that contemplated under the plans filed than from any new concept as to the fully secured position of the Finance Corporation. The approval of the issue of new first-mortgage bonds to

the Finance Corporation, while the debtor's bondholders are to receive none of such bonds, is justified, in our opinion, by considerations beyond the estimated value of the particular securities under pledge. Not only is the Finance Corporation in possession of the stocks of the Salt Lake and the Salt Lake Western, and thus in position to veto the consolidation of properties which forms the basis of the plan, but it has indicated that it will, if satisfied with the plan, agree to underwrite the financing necessary to redeem the Salt Lake bonds outstanding in the hands of the public, the payment of trustee's certificates, and the cash required for reorganization expenses, etc., a total of $17,443,675.

It is probable that under present conditions the new first-mortgage bonds of the reorganized company would not be salable at par, and the Finance Corporation should be compensated in some manner for acceptance of them at par in return for furnishing the $17,443,675 of cash necessary to carry out the plan. But clearly such compensation should not be limited to the probable present deficiency in the market value of the bonds. A practicable development of the procedure for placing the plan in effect will require a definite commitment by the Finance Corporation prior to the referendum on the plan, and from six months to a year probably will elapse after such commitment before the Finance Corporation will be called upon to supply the funds. At the approximate time of the financing, the transaction must receive our approval under section 5 of the Reconstruction Finance Corporation Act. What the market value of the securities may be at that time obviously cannot now be forecast.

In view of these circumstances, we approve the exchange of new first-mortgage 4-percent bonds, series A, in the approximate amount of $11,959,469 in settlement of the claims of the Finance Corporation for principal and interest accrued to June 30, 1938, such arrangement, however, to be conditioned upon agreement by the Finance Corporation to purchase, at par, approximately $11,443,675 of series-A bonds, the proceeds to be used for the purpose of redeeming the $11,234,000 of Salt Lake first-mortgage bonds and income bonds outstanding, and further to purchase approximately $6,000,000 of such bonds for the purpose of paying the debtor's trustees' certificates outstanding, the expenses of the reorganization, and for working capital. In the event of failure of the Finance Corporation to file with the court, prior to a referendum on the plan, a commitment to supply the new money under the above-prescribed terms, the plan should be considered to be impracticable, and should be returned to us for further consideration.

Means of future financing.—In the debtor's plan, the means of future financing by the new company, with respect to requirements not covered by the additions and betterments fund and new equipment-trust obligations, are provided through bonds to be issued under any of the proposed mortgages, as well as through the new preferred stock. Counsel for the committee take the position that first-mortgage bonds offer the lowest yield and provide the cheapest forms of financing; that the preservation of a sound capital structure will be insured if the new mortgage imposes proper limitations as to the purposes and amounts of additional issues; that fixed-interest bonds issued under such conditions and the limitations prescribed in section 77 provide a continuing medium for investment in railroad securities by trust funds and trust institutions, and thus broaden the market for cheap credit. Counsel further contend that there is no necessity for a sinking fund for the retirement of bonds issued under an open first mortgage, such as is contemplated, and that any reduction in the amount of bonds issuable in order to provide for a sinking fund would be unjustifiable, "since it would require the bondholders to pay off their own debts for the benefit of the equity."

Counsel urge that, in the case of income-mortgage bonds which are issued to present bondholders having a vested contract right to the payment of both principal and interest, creditors receiving such bonds are entitled to the payment of the principal as soon as it may be done without prejudice to the property. Accordingly, a sinking fund for the retirement of income bonds, issued under a closed mortgage, is considered by them to be desirable, provided the annual payments are made after payments to the capital fund and of contingent interest.

While we consider the committee's proposal for the early retirement of the income bonds a proper one, it is doubtful that the financing medium of the new company by bonds should be restricted to first-mortgage fixed-interest bonds. The plan herein approved provides for a relatively small initial issue of such bonds and otherwise departs from the committee's plan, owing to a different consideration of the earning power of the property, as has been stated. We believe that it will be in the interest of the new company to have both the first mortgage and income mortgage open, with proper restrictions as to the purposes for which additional bonds may be issued.

Equity, future control.—The debtor's contention that the present stockholders have a substantial equity is based on the recorded investment in the property, the recent improvements, which are

expected to increase net revenues, and the alleged potential earning power of the road. Counsel argue that the bankruptcy of the company was a temporary condition due to the heavy investment in the cut-off, that depression earnings should not govern in determining the equity of the stockholders, that no consideration should be given to our valuation of the physical property, that real value can be fixed only by means of a sale, and that an administrative body has no power to foreclose a property interest by an appraisement. Counsel for the debtor believe that section 77 is a composition statute, under which an agreement with the creditors is contemplated, such agreement being subject to our approval only from the standpoint of fairness and the public interest.

Section 77 provides, among other things, that the plan must afford due recognition to the rights of each class of creditors and stockholders. In *New York, N. H. & H. R. Co.*, 16 Fed. Supp. 504, 511, *Northern Pac. Ry.* v. *Boyd*, 228 U. S. 482, 505, and other cases, the courts have ruled that the claims of bondholders holding liens on the property of a bankrupt estate must be satisfied before consideration can be given to the rights of the stockholders. In our opinion, section 77 contains no provision which is contrary to the law of the land in respect of the relative rights and priorities involved in such a case as this. The rights of creditors and stockholders may be modified under the provisions of section 77 (b) but certainly not in violation of recognized priorities as between senior and junior interests. It follows that we must consider the aggregate amount of the claims of the bondholders and other secured creditors in the light of the earning power of the system, past, present, and prospective, and all relevant facts, in order to determine the equity of any class of stockholders, this being essential to the findings which we may be called upon to make under section 77 (e) in connection with the question of submitting the plan to the stockholders. The requirements as to such findings are not consistent with freedom of the debtor to make an agreement with its creditors for a composition of their claims or with the assumption that the debtor's interest shall remain undisturbed regardless of the apparent insolvency of the company. If the evidence clearly indicates no equity for the present stockholders, we are unable to find justification for their participation in the plan.

Referring to the balance sheet of December 31, 1936, which is the latest one contained in the record, the capital liabilities of the Denver, other than capital stock, together with total current liabilities, deferred liabilities, tax liability, government grants, and other unadjusted credits, amount to $154,552,730. Deducting all book assets, other than those representing investments, the net

amount was $140,560,266. For the combined properties, after intercompany eliminations, the corresponding figure was $153,314,502, which represents the net debt of the system on the basis of the consolidated balance sheet.

The decline in earnings was most marked between 1931 and 1932. Considering the Denver's operation alone, the average income available for interest during the 5-year period 1927–31 was $7,090,618 a year. During the next four years, 1932–35, adopted as a basis for the committee's plan, the Denver's average available income was $3,025,728. During the succeeding three years, 1936–38, the average was only $685,974. As of January 1, 1937, the effective date of the plans presented, the Denver's total debt, including unpaid interest, amounted to about $146,262,723, and the annual charges on the principal only were $5,762,392 per annum. As of June 30, 1938, the effective date of this approved plan, the total debt, including interest, had increased to $160,140,879 and the annual charges to $5,919,227. In no year since 1930 have the Denver's earnings been equal to such charges. The Denver's part of the test period earnings was $2,431,217, and its part of the predicted earnings in the future normal year was $5,198,318. In no year has the present Denver Company paid a dividend on either class of stock.

Since the Denver controls the Salt Lake through ownership of over 99 percent of its capital stock, the combined earnings in connection with the combined debt may be considered as bearing upon the value of the equity of the Denver's stock. On this basis the average system income available for interest was $8,103,881 during the five years 1927–31, $3,606,921 during the four years 1932–35, and $1,128,869 during the three years 1936–38. The total system debt increased from $157,496,723 as of January 1, 1937, to $171,374,879 as of June 30, 1938, while the annual charges on the principal increased from $6,406,432 to $6,563,267. As in the case of the Denver alone, these charges have not been earned in any year since 1930, and are not equaled either by the earnings of the test period or by those shown for the normal year. There is no evidence in the record indicating any probability that the carriers can bring their earnings up to the 1930 level or to that of the 1927–31 average, and in our opinion such former earnings should not be relied upon as the measure of an earning power justifying a finding that the equity in the debtor's stock has a value. The forecast for a future normal year, showing $6,215,423 as the system income available for interest, compares with about $8,000,000 earned in 1930 and a slightly larger average amount in 1927–31. The forecast figure, if capitalized at 4½ percent, approximates $138,000,-

000, while the total debt exceeds $171,000,000. The reproduction-cost figure of $147,717,268 has been referred to. From all these considerations we find that the equity of the owners of the debtor's common stock and its preferred stock has no value and that the holders of claims in classes 1 and 2 are not entitled to participate in the plan.

While the Insurance Group committee concluded that there is no equity in either class of the debtor's stock, it proposed that the proprietary companies be given precedence in the right to acquire effective control of the new company by purchase of the proposed class-B common stock, as had been described. The Western Pacific is not represented in this proceeding, but the representatives of the debtor, the Missouri Pacific, numerous civic bodies, and others have strongly urged that our plan provide a means whereby the proprietary companies may retain control of the Denver through acquisition of a majority of the new voting stock. They contend that the plan would not meet the requirement of public interest unless it contained such a provision. The evidence in this connection includes facts as to the long-established through route via the Missouri Pacific, the Denver, and the Western Pacific, the dependence of the Missouri Pacific's line between Osawatomie and Pueblo on the through traffic which has been developed, the need of the Denver for both the Denver gateway and the Pueblo gateway, the grouping of the Missouri Pacific, the Denver, and the Western Pacific under our consolidation plan *(Consolidation of Railroads, supra)*, our approval of the acquisition by the Missouri Pacific from the Western Pacific of a half interest in the Denver's stock *(Denver & R. G. W. R. Co. Reorganization,* 82 I. C. C. 745), and other matters. It has been argued that to divide the proprietary interest in the Denver between the present stockholders and other trunk lines as suggested by the committee would destroy the existing working arrangement and result in injury to the Denver.

As we view the matter these are not questions for us to decide in promulgating a reorganization plan where we find that the present stockholders have no equity, and we do not consider it our duty in this case to decide for the new owners what affiliations with other systems will be most advantageous to the new company, or to fix a price for any stock which may be offered to the Missouri Pacific, Western Pacific, or other railroad companies. In order, however, to facilitate any reasonable plan which the new stockholders may adopt with respect to the acquisition of an interest by a larger system or systems, the following provision for the stock should be incorporated in the reorganization plan. All the common stock issued by the new company in the reorganization, excepting shares

issued to qualify directors, should be deposited under an escrow agreement with a bank or trust company designated by the court and escrow receipts issued to the persons entitled to receive such stock under the plan. The escrow agreement should be for a term of 10 years from July 1, 1939, and should provide that the reorganization committee, as voting trustees, may, subject to our approval, and with the consent of the holders of escrow receipts representing a majority of the shares on deposit, sell all or any part of such deposited common stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders. It should be provided that all holders of escrow receipts will be bound by the terms of any sale which shall have been approved by us and consented to by the holders of escrow receipts representing a majority of the total number of shares issued, and that the new proceeds of any sale, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts. During the life of the escrow agreement, the holders of escrow receipts should have the right to receive notice of all meetings of stockholders and to direct the reorganization committee as to the manner in which the stock represented by such escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stock should be voted in such manner as the reorganization committee may determine.

Allocation of new securities.—In order to establish a distribution of the test-period earnings conforming to the conclusions reached above, the debtor's basic distribution (exhibit 109, note A) is adjusted to transfer the group of equipment in dispute from the refunding and improvement mortgage, as shown in the committee's formula, and to cancel the loss on the refunding and improvement mortgage branches and allow a return of 4 percent per annum on the standard-gage equipment subject to the lien of that mortgage, as shown in the computations made by the trustee. The resulting figures, representing test-period income available for interest, are as follows:

R. G. Western first-trust mortgage	$1,122,050
R. G. Western consolidated mortgage	[1] 88,419
Junction first mortgage	164,563
D. & R. G. consolidated mortgage	978,628
Equipment trusts	131,519
D. & R. G. W. refunding and improvement mortgage	333,297
R. F. C. collateral (earnings of the cut-off, Salt Lake's operation, motor carriers)	1,284,585
	3,926,223

[1] Deduction.

Referring to the last item above, if the interest requirement of the debt to the Finance Corporation, together with that of the new bonds to be issued for the redemption of the Salt Lake bonds, be subtracted from the allocated earnings of $1,284,585, an excess of $348,359 remains, which, in our opinion, should be distributed among the three mortgage divisions where the interest requirements were not covered by earnings, viz, the R. G. Western consolidateds, the D. & R. G. consolidateds, and the refunding and improvements, and should be distributed in proportion to their respective deficiencies. When this is done the earnings, other than those of the Finance Corporation division and the equipment trusts, are as follows:

	Percent
R. G. Western first-trust mortgage, $1,122,050	39.3
R. G. Western consolidated mortgage, $32,496	1.1
Junction first mortgage, $164,563	5.8
D. & R. G. consolidated mortgage, $1,124,632	39.3
D. & R. G. W. refunding and improvement mortgage, $414,837	14.5
	100.0

If the above percents be applied to $42,000,000 of new income-mortgage bonds, being the approximate aggregate amount of such bonds which we find to be justified by existing conditions, the resulting amounts would bear the following relations to the amounts of the five claims, respectively: R. G. Western first trusts, 95.3 percent; R. G. Western consolidateds, 2.7 percent; Junction firsts, 105.5 percent, D. & R. G. consolidateds, 35 percent, and D. & R. G. W. refunding and improvement mortgage bonds, 36.5 percent. The distribution of new income bonds, shown in the attached appendix, is in substantial accord with these percents and in our opinion provides for an equitable treatment of the several claims based on the data available.

The new company should assume the equipment obligations of the present companies, or their trustees, at the consummation of the plan. We find that the interests of the holders of equipment obligations will not be adversely and materially affected by the plan of reorganization approved by us, and submission of the plan to such holders is not necessary. The issue of additional equipment obligations prior or subsequent to the consummation of the plan, if duly authorized under section 20a of the Interstate Commerce Act, is not prohibited under the plan herein approved.

The holders of bonds of the classes stated below should receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, the following approximate amounts of new securities: R. G. Western first-trust bonds, $1,140 of new

4½-percent income bonds; R. G. Western consolidated-mortgage bonds, $1,150, par value, of new 5-percent preferred stock; Junction first-mortgage bonds, $1,154 of new 4½-percent income bonds; D. & R. G. consolidated-mortgage 4-percent bonds, $406 of new 4½-percent income bonds, $290, par value, of new 5-percent preferred stock, and 4.64 shares of new common stock; D. & R. G. consolidated-mortgage 4½-percent bonds, $413 of new 4½-percent income bonds, $295, par value, of new 5-percent preferred stock, and 4.75 shares of new common stock; D. & R. G. W. refunding and improvement mortgage 5-percent bonds, $416 of new 4½-percent income bonds, $297, par value, of new 5-percent preferred stock, and 4.75 shares of new common stock; D. & R. G. W. refunding and improvement mortgage 6-percent bonds, $429 of new 4½-percent income bonds, $306, par value, of new 5-percent preferred stock, and 4.9 shares of new common stock; D. & R. G. W. general-mortgage bonds, 4.15 shares of new common stock. The holder of each $1,000 Junction first-mortgage bond should receive, in addition, a cash payment of $14.17, representing 17 months' interest on such bond at 1 percent.

The foregoing amounts of new securities, being mostly in odd figures, owing to the accumulations of interest on the present bonds and other circumstances, will require the issue of scrip for sums less than $100 in the case of bonds, and for fractional shares of stock. Provision for the issue of such scrip should be made in the plan.

The holders of the 460 shares of stock of the Salt Lake outstanding in the hands of the public should receive, in exchange therefor, $46,000, principal amount, of new 4½-percent income bonds. The system earnings of the test-period year, as computed by the committee, correspond to approximately $4.21 a share for the Salt Lake stock, but the highest actual earnings of the Salt Lake in any one year since 1929 were only $1.79 a share, and in other years since 1929 they were much less than $1 a share. One intervener computes the test-period earnings on the Salt Lake stock at $8.07 a share after giving effect to the estimated savings from consolidation, as well as the savings through the proposed refunding of the Salt Lake bonds on a 4-percent basis. While the proper treatment of this stock is debatable, the use of the test-period earnings is consistent with the approved plan, on which basis we consider the allocation of new income bonds to this claim, as proposed in the debtor's plan, to be fair.

The secured note held by the Railroad Credit Corporation should either be paid in cash or be extended, at the discretion of the reorganization committee. If the latter plan be adopted, the note

of the new company should be in face amount equal to the indebtedness to the Credit Corporation, after any distributive credits which may apply thereon, bearing interest at the contract rate per annum, and payable in 6 months from the effective date of the plan. The new securities issuable as collateral for such note, representing those for which the present collateral with accumulated interest would be exchangeable under this plan, would consist of $268,772 of new income bonds, $191,980 of new preferred stock, and 3,072 shares of new common stock. Upon payment of such note the pledged securities should be canceled. Nothing in the foregoing provisions is intended to limit or in any manner affect the right of the Railroad Credit Corporation to apply, in its discretion, the income on and proceeds of the collateral held by it to or toward the payment of the principal or interest, or both, of or upon its claim against the debtor prior to the consummation of the reorganization.

The secured note held by the Chase National Bank should be canceled and a new note or new notes issued in face amount equal to that of the present note, plus interest accrued to June 30, 1938, in the amount allowed by the court, such notes to mature in 10 years, subject, however, to renewal or renewals from time to time at the option of the new company for further periods of 10 years each until retired in the manner to be set forth in the agreement securing such notes. Such notes should bear interest at the rate of 4 percent per annum, payable semiannually on October 1 and April 1 of each year, but such interest should be contingent on, and payment thereof should be limited to, the total of the interest and dividends paid by the new company on the collateral securing such notes. The interest should be cumulative to the maximum amount at any one time of 16 percent, whether for consecutive or nonconsecutive income periods. Any interest and/or dividends paid upon the pledged collateral in excess of interest requirements on such notes, including accumulations of interest, should be applied to the payment of the principal amount of such notes. Such notes may be redeemed in whole or in part at any time on 30 days' notice at their principal amount plus full interest at the rate of 4 percent per annum accrued since the last preceding April 1, and all unpaid accumulated interest. Upon the payment or other retirement of all such notes, the collateral securing them should be returned to the new company, and the new company should, in the case of certificates of stock, cancel and retire the same, and in the case of bonds deliver the same forthwith to the trustee under the indenture securing the same for cancelation and retirement; no bonds should be issued in lieu of any bonds so canceled and retired. The

new securities issuable as collateral, representing those for which the bonds now pledged, with accumulated interest to the effective date of the plan, would be exchangeable under the approved plan, would consist of $2,533,650 of income bonds, $1,809,750 of preferred stock, and 28,956 of common stock.

As has been stated, the Salt Lake bonds should be called for redemption as a part of the plan, the call price for the first-mortgage 4's being 101 and that for the income-mortgage 6's being 102. The trustees' certificates outstanding, which represent a lien prior to the lien of any of the mortgages issued or assumed by the debtor, should be paid in cash. Additional cash in the approximate amount of $1,000,000 should be provided for the payment of the expenses of reorganization and for working capital. As the needs of the company at the time the reorganization may be effected are not ascertainable, the provision for $1,000,000 of cash is necessarily tentative. The total requirements mentioned in this paragraph aggregate approximately $17,443,675, against which a like amount of new first-mortgage 4-percent bonds are shown in the plan schedule. In discussing the claims of the Finance Corporation we have already stated that a commitment should be obtained from that corporation obligating it to provide the financing described by taking the new first-mortgage bonds at par as a condition of the issue of new first-mortgage bonds for the full amount of the claim of the Finance Corporation.

As of December 31, 1936, there were outstanding $278,297.50 of coupons on bonds and equipment-trust certificates which had not been presented for payment prior to November 1, 1935. The cash item in the balance sheet included $105,891.06 for the payment of bond coupons. In the absence of later information it is assumed that not all these coupons will have been presented at the consummation of the reorganization and that the plan should make provision for them. Our order of approval will provide that such coupons shall be paid in cash by the new company if and when presented by the holders thereof.

Securities issued in the reorganization of 1924, which have not been claimed, should receive new securities under the plan herein approved, to the same extent as like outstanding securities of the Denver, or a cash settlement, as may be determined by the court.

Miscellaneous provisions.—The new company should assume liability for and pay in due course any and all taxes due to the United States from the debtors or their trustees or any of their subsidiaries, for any taxable period prior to the date of confirmation of the

plan, without proof thereof and without prejudice by reason of not having been proven.

As has been stated, the Moffat Tunnel Improvement District raised various objections to the plans of reorganization presented insofar as they provide for the merger or consolidation of the Salt Lake with the new company. It questions the authority of the court and this Commision to include in a plan of reorganization provision for the merger or consoiidation of the Salt Lake with the properties sought to be reorganized, on the ground that that corporation is solvent, is not a debtor herein, and a majority of its capital stock is pledged with the Finance Corporation as security for loans, with voting rights in the pledgee. Section 77 (b) describes in comprehensive language the subject matter which a plan of reorganization may embrace, stating that it may include "the merger or consolidation of the debtor with another corporation or corporations." We do not construe this to mean that every corporation that may be merged or consolidated with another by the plan need be a debtor or that its property need be subject to the jurisdiction of the court in the proceeding, provided that appropriate corporate action be taken by the nondebtor corporation.

The Tunnel District also takes the position that by reason of the existing lease for the use of the railroad tunnel the Salt Lake does not have the right by voluntary corporate action to cause its properties to be merged or consolidated with those of another corporation, contending in effect that the lessor is entitled to look to the property of the lessee as a trust fund for the payment of rent provided under the lease. We are not persuaded that these are legal consequences resulting from the lease. In *Kansas City Term. Ry. Co.* v. *Central Union Trust Co.*, 294 Fed. 32, the Circuit Court of Appeals, Eighth Circuit, held that contracts between railroad companies relating to joint ownership, maintenance, and use of a union station, which did not purport to be mortgages or to convey any title or interest in the properties of the several companies, did not create a lien on the general property of a company which took precedence of a subsequent mortgage and did not create covenants which ran with the property of the several companies and followed it into the hands of subsequent purchasers. In *Wabash, St. L. & P. Ry. Co.* v. *Ham*, 114 U. S. 587, the Supreme Court took occasion to discuss the so-called trust-fund theory in holding that equipment-trust obligations unsecured by any mortgage of a railroad company which subsequently consolidated with other corporations did not create a lien upon the properties of the consolidated company. Justice Gray said, in part:

The property of a corporation is doubtless a trust fund for the payment of its debts, in the sense that when the corporation is lawfully dissolved and all its business wound up, or when it is insolvent, all its creditors are entitled in equity to have their debts paid out of the corporate property before any distribution thereof among the stockholders. It is also true, in the case of a corporation, as in that of a natural person, that any conveyance of property of the debtor, without authority of law, and in fraud of existing creditors, is void as against them. * * *

But upon the consolidation, under express authority of statute, of two or more solvent corporations, the business of the old corporations is not wound up, nor their property sequestrated or distributed, but the very object of the consolidation, and of the statutes which permit it, is to continue the business of the old corporations.

The Tunnel District contends further that any transfer by the Salt Lake to the reorganized and consolidated company of its property and the lease would not be legal in view of a provision in the act of the legislature of the State of Colorado authorizing the construction of the tunnel and regulating its uses which reads:

All contracts may be assigned or subleased, *provided*, that the original contracting parties shall not be thereby relieved of any obligations under said contract or lease.

The lease, however, makes provision that successors and assignees of the lease shall be bound by the terms of the lease and that the lessee shall be released therefrom upon approval of said assignments by the lessor. This provision of the lease and the quoted portion of the statute were construed by the Circuit Court of Appeals, Tenth Circuit, in *Moffat Tunnel Improvement Dist.* v. *Denver & S. L. Ry. Co.*, 45 Fed. (2d) 712. That court stated its conclusions thereon as follows:

The powers conferred upon the [Moffat Tunnel] Commission undoubtedly are broad enough to permit it to cancel an existing lease with the consent of the lessee, and make another. The clause objected to amounts to that; it may release the Railway in case of a sale of its properties, but it is not required to. Such clause does not render the lease void.

We do not believe that the statute which declared, in effect, that the tunnel should be put to the greatest possible use, and that leases should be assignable, could be construed to prevent a lessee such as the Salt Lake from consolidating its property under appropriate State and Federal authority with a large railway system, such as that of the principal debtor, and having the reorganized and consolidated company assume responsibility for the performance of the lease. The Tunnel District requests that we suggest some method in connection with a plan of reorganization by which the district, if it should cancel the present lease and make a new

one with the consolidated corporation, may receive the same measure of security which it now has from its present solvent lessee. This we are endeavoring to do. The capital structure under the plan we approve herein we believe requires conservative fixed charges in the light of the probable earning power of the properties. Rentals due under the lease of the tunnel will, of course, be payable as a fixed charge before any interest would be payable on the bonds of the new company. We have issued numerous reports and orders describing the purposes of the tunnel and opening the way for more complete use of it for railroad purposes. It is our view that a long-range view of its purposes and possibilities should not be obstructed by placing too much emphasis upon the solvency of the present lessee. In the last analysis, the success of that carrier is closely allied with the system with which it is now connected through stock ownership.

The new company may take any action with respect to the lease or agreement with the Northwestern Terminal Railroad Company as may be lawful under the terms thereof. As to all other agreements and executory contracts, including the existing lease agreement of the Salt Lake with the Moffat Tunnel Improvement District, the new company should be deemed to have assumed the obligations with respect to such agreements and contracts which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding and which shall not have been disaffirmed by the trustees of the respective estates with the approval of the court prior to confirmation of the plan, and the new company should also assume any executory contracts made by the trustees, with the approval of the court, which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding

Claims against the debtors and their subsidiaries entitled to priority over their respective mortgages, claims for taxes levied, assessed, or accrued against the debtors, their subsidiaries, or trustees, current liabilities and obligations incurred by the trustees during the reorganization proceedings, to the extent unpaid at the date of confirmation of the plan, and claims arising from the disaffirmance of executory leases or contracts of the trustees pursuant to orders of the court, in respect of which claims are filed or evidenced in accordance with orders of the court, should be assumed by the new company and paid in the usual course of business with the same relative priority as they now have with respect to other obligations of the debtor or its subsidiaries. When so treated, we find, such claims against the debtors, other than the obligations of trustees, and the interests of parties to agreements

and executory contracts with the debtors assumed by the new company, are not adversely and materially affected by the plan.

The holders of unsecured claims against the debtors arising prior to the filing of the petitions under section 77, not entitled to priority, should receive new common stock on the basis of one share for each $200 of claim allowed by the court.

We are of the opinion that a reorganization committee is necessary to carry out the plan and that it should consist of five members, two to be designated by the Insurance Group committee as representatives of the R. G. Western first-mortgage bonds, the Junction first-mortgage bonds, the D. & R. G. consolidated-mortgage bonds, and the R. G. Western consolidated-mortgage bonds, one to be designated by the trustee under the Denver's refunding and improvement mortgage, one by the trustee under the Denver's general mortgage, and one by the Finance Corporation as its representative. The reorganization committee may fill any vacancies created by death, resignation, or otherwise, preserving the representation of the several interests as before. The members of the committee should agree to serve without compensation, but its expenses should be paid by the new company, subject to the provisions of section 77 and the approval of the court, as part of the cost of the effectuation of the plan.

The reorganization committee should not be authorized to solicit deposits of securities or authorizations to represent security holders, except upon approval by us of the terms of such solicitation, pursuant to section 77 (p) of the Bankruptcy Act, as amended.

The method and procedure for effectuating the plan should be determined by the reorganization committee in its discretion, and the committee should also determine the form, and, to the extent not inconsistent with the plan herein approved, the provisions of all mortgages, bonds, coupons, charters, bylaws, stock certificates, escrow agreements, and all other instruments necessary or desirable in connection with the effectuation of the plan, subject to the extent now or at the time provided by law to the approval of the court and of this Commission, or other tribunal having jurisdiction in the premises.

The number of directors of the new company and the manner of their election should be determined by the reorganization committee and provided for in the new charter or in an amendment of the debtor's present charter.

The plan should be carried out by vesting the properties of the Denver and its affiliated companies, together with the property held by the trustees, either in the reorganized Denver corporation or in a new corporation created for the purpose of this reorgani-

zation, and by the execution by the reorganized or new company of the new mortgages and the issue by it of the new securities contemplated under the plan. The reorganized or new company should be deemed to have come into possession of the properties as of the effective date of the plan, June 30, 1938. The merger or consolidation of the Salt Lake should be effected in a manner to be determined by the reorganization committee, subject to our approval and that of the court.

The expenses of reorganization, as allowed by the court, subject to the provisions of section 77, should be paid in cash or assumed by the new company as a cost of administration prior in lien to the new securities issued under the plan.

In connection with the plan proposed by the Insurance Group committee we described the suggested provision for a sale of the debtor's and secondary debtor's properties in the event the holders of more than one-third in principal amount of any class shall not have accepted the plan within a period to be fixed by the reorganization committee. Such a provision may properly be adopted, since section 77 authorizes inclusion in a plan, as part of the provisions for it execution, a sale of all or any part of the property of a debtor at not less than a fair upset price, etc. We are unable to approve, however, the sale provision as suggested by the committee, and are of the opinion that the following provision is appropriate in this case.

If so ordered by the court, the plan, after it has been found fair and equitable and has been confirmed by the court, may be executed by the sale or sales, at not less than fair upset prices, to be fixed by the court, of all or any part of the property of the debtor and the secondary debtor, all on such conditions and in such manner as the court may direct. Upon any such sale or sales, the property and assets offered for sale may be purchased for the benefit of the new company by the reorganization committee, and in that event there shall be applied on account of the purchase price the distributive share of the proceeds of such sale of all securities the holders of which shall have assented to the plan, and of the securities, though not assenting to the plan, of all classes which shall have accepted the plan. If the property of the debtor or secondary debtor, or both, so offered for sale should be sold to others than the reorganization committee, the plan herein approved shall be deemed inoperative except insofar as provision is made therein for the sale of the properties as may be ordered by the court.

In the event of any such sale to the reorganization committee, it may in its discretion sell all or any portion of the new securities distributable under the plan in respect of securities of any creditor,

if neither such creditor nor the class to which such creditor belongs shall have accepted the plan, provided that creditors in a class which shall not have accepted the plan, and who themselves shall not have accepted the plan, shall have the right, if they shall so notify the committee within a period of 30 days after the confirmation of the sale, to assent to the plan and receive the securities allocated to them under the plan in lieu of their aliquot share of the proceeds of such sale. The proceeds of sale of securities may be used to pay the portion of the purchase price payable in cash on any such sale of the properties.

We find that the plan of reorganization and consolidation herein described, which differs from any of the plans presented, will meet with the requirements of subsections (b) and (c) of section 77 of the Bankruptcy Act, as amended, and will be compatible with the public interest. Modification of the accounts of the debtor and the other companies involved, as a result of the plan finally adopted, should be subject to our approval, and the new company should submit its journal entries for such approval before making its permanent accounting records.

In view of the provisions of subsection (f) of section 77, we will give consideration, when a plan is finally adopted, to the granting of such authorization as may be requisite and appropriate for the execution of the plan, including the issue of securities.

An appropriate order will be entered.

EASTMAN, *Chairman*, concurring in part:

I concur, except as indicated in my separate expression in *Western Pac. R. Co. Reorganization*, 233 I. C. C. 409, decided June 21, 1939.

MILLER, *Commissioner*, concurring in part:

It is apparent to me that the total capitalization authorized in this proceeding is too high, particularly when measured by the original cost of the property, less depreciation.

For reason stated in my separate expressions in previous reorganization cases, I do not approve a mandatory capital fund. *Western Pac. R. Co. Reorganization*, 233 I. C. C. 409.

My remarks regarding the desirability of setting up sinking-fund payments in terms of a percentage of earnings, conditions regarding the issuance of fixed-interest bonds, a participation provision rather than a cumulative requirement for income bonds, and the use of no-par-value preferred stock, are equally as applicable to this case as to those in which they were made. *Spokane Interna-*

tional Ry. Co. Reorganization, 233 I. C. C. 157, and *Western Pac. R. Co. Reorganization*, *supra*;

SPLAWN, *Commissioner*, concurring in part:

I agree with the findings of probable earnings for the future. The discussion of priorities is difficult to follow. Apparently an effort is made to substitute for bonds on which interest is now being earned a security which will obviously have much less value. It is not made clear that such a substitution would be lawful.

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted December 1, 1939. Decided April 2, 1940

Upon further consideration, plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, modified and approved.[1]

Appearances as in prior report, and *A. Marvin Braverman, Claude E. Hamilton, Jr., A. M. Lewis, Curtis Heath, Samuel M. January,* and *George John Miller.*

Report of the Commission on Further Consideration

BY THE COMMISSION:

By our report and order of July 11, 1939, in this proceeding, 233 I. C. C. 515, we approved a plan of reorganization for The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor. Proceedings for reorganization of these companies are pending in the United States District Court for the District of Colorado. The plan provides that the properties of the debtor, the secondary debtor, The Denver and Salt Lake Railway Company, The Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company should be merged or consolidated by transfer of the subsidiary properties to the reorganized debtor or by transfer of all the properties to a new corporation organized for the purpose. The abbreviated titles used in our prior report will be used herein.

On or about September 9, 1939, petitions for modification of the approved plan were filed by (1) George S. Van Schaick et al. as the executive committee of a group of life-insurance companies,

[1] Previous reports, 212 I. C. C. 105 and 709, 217 I. C. C. 191, 224 I. C. C. 574, and 233 I. C. C. 515. Orders entered without report (other than orders permitting interventions), January 21, August 8, and September 4, 1936, January 9, April 12, May 26, and October 27, 1937, May 26 and November 28, 1938, and October 12, 1939; certificate, December 20, 1939.

known as the insurance-group committee, (2) Guy A. Thompson, trustee of the Missouri Pacific Railroad Company, (3) the Central Hanover Bank & Trust Company, trustee under the first-trust mortgage of the Rio Grande Western Railway Company and the first mortgage of the Rio Grande Junction Railway Company, (4) the United States Trust Company of New York, trustee under the consolidated mortgage of the Denver & Rio Grande Railroad Company, (5) the Guaranty Trust Company of New York, successor trustee under the first consolidated mortgage of the Rio Grande Western Railway Company, (6) the City Bank Farmers Trust Company, trustee under the general mortgage of the Denver & Rio Grande Western Railroad Company, (7) the Moffat Tunnel Improvement District and the Moffat Tunnel Commission, and (8) the Security Research Bureau, all interveners herein, and by (9) the debtor and its subsidiaries.

Certain interveners requested that the proceeding be reopened for further hearing, if such further hearing was deemed necessary by us, and that permission be given to file briefs and to present oral argument in support of the petitions. By order of division 4, all parties to the proceeding were permitted to file briefs on or before November 15, 1939, and reply briefs on or before December 1, 1939. Briefs were filed by the insurance-group committee, the Central Hanover Bank & Trust Company, the United States Trust Company of New York, the Guaranty Trust Company of New York, the City Bank Farmers Trust Company, the debtor, and the Untermyer family group; and reply briefs were filed by the Chase National Bank of the City of New York, the Finance Corporation, the Security Research Bureau, and the Moffat Tunnel Improvement District and the Moffat Tunnel Commission. We have given careful consideration to the questions raised by the parties and the modifications of plan requested.

Of chief importance among the modifications sought is that asking us to eliminate from the plan all provisions for consolidating the debtor with its subsidiaries. In urging this change, the insurance group committee contends that a consolidation of the Salt Lake with the Denver, in connection with the reorganization, upon the terms approved by us, is illegal and impracticable, and that any attempt to consolidate these roads and the Salt Lake Western should be abandoned. The committee presents a new plan, showing the amount of each class of new securities and the allotments to present creditors on the basis of the earnings formula, adjusted to eliminate the Salt Lake and the cut-off. The plan provides that the lease of the Salt Lake Western and the trackage agreement between the Salt Lake and the Denver be disaffirmed and rejected

as of November 1, 1935. It is stated that no serious consideration need be given to any substantial claim which may arise from such disaffirmance and rejection, since the assets and prospects of the Denver do not permit any recognition of the claims of general creditors unsecured by lien.

The committee now suggests that normally, under principles applicable in the marshaling of assets, the Finance Corporation would be merely a general creditor and should not be permitted to participate in the reorganization or even to foreclose on Denver securities held as collateral, except to the extent that the part of the pledged collateral in which other creditors have no interest may prove insufficient to satisfy the claim. The stocks of the Salt Lake and the Salt Lake Western are regarded by the committee as such part of the collateral in which other creditors have no interest, and the testimony of the Finance Corporation's witness is cited to show that the loan is fully secured by these stocks. But, should this part of the collateral prove insufficient, the committee evidently recognizes the right of the Finance Corporation to receive the securities of the new company allocable in respect of the debtor's bonds pledged with the Finance Corporation, on the same basis as the other holders of like bonds. The plan in fact shows specific amounts of new bonds and stocks issuable against the pledged securities (other than the aforesaid stocks and the motor companies' stocks); likewise new securities issuable against the bonds pledged with the Railroad Credit Corporation and the Chase National Bank, and all such new securities are included in the suggested new capitalization of the Denver.

While the committee states that the new corporate management of the Denver would be free to take any steps that it may deem proper for the acquisition of the Salt Lake and the Salt Lake Western, and that there is no intention to obstruct an ultimate unification of all the properties, the committee asserts that we have no authority to alter the rights or impair the priority of any prime mortgage liens on the properties of the Denver or the Junction for the sole purpose of effecting a consolidation, as we allegedly attempt to do under our approved plan. The committee refers to the fact that a consolidation can be effected only by voluntary agreement of the interested parties. Its position is that its original plan accorded treatment to the Denver's bondholders in accordance with their relative priorities, and that such plan would be acceptable to the bondholders and the Finance Corporation, whereas under the plan approved by us the capitalization of the new company, the amount of fixed charges permitted, and the treatment of the Finance Corporation are unfair and inequitable, making the plan

impossible of acceptance. The committee evidences its active opposition and believes that such opposition will be general and that the plan is therefore impracticable and if certified to the court will cause extended litigation, expense, and delay.

Several interveners agree with the committee's proposal in principal, including the Chase National Bank, trustee of the debtor's refunding and improvement mortgage. The bank, in its capacity as mortgage trustee, did not file a petition requesting modification of the approved plan, but filed an answer to the committee's petition and a brief in which the structure of the committee's plan was analyzed and various modifications suggested, such as the allowance of some form of arbitrary to the cut-off representing a fair division of rates as between separate railroads. No party accepts the committee's proposed allotment of securities.

We wish to point out that the committee has no ground for an assumption that we would approve, in any event, a plan and a new capital structure such as the committee has promulgated for the Denver alone. Both of the plans presented for our approval contemplated the consolidation provided for in the plan approved by us, although on different terms. All parties to the proceeding supported such consolidation, and the record before us was made in contemplation of such an arrangement. We are not prepared to say that the capitalization which we might consider proper on this new basis would permit substantially better treatment of the Denver's bondholders than does the plan approved on the basis of a consolidation of all the properties.

It would seem that a disruption of the present intercompany agreements and an indefinite postponement of the benefits of unified operation and management should be considered in connection with the bondholders' ultimate interest. Consideration should also be given to the amount and probable value of the Salt Lake and Salt Lake Western stocks, together with the various new securities, which the committee now proposes to assign to the Finance Corporation for its claim of approximately $12,000,000. The committee and other interveners complain that under our plan the bondholders would pay too high a price for the effectuation of consolidation, but the proposed modified treatment of the Finance Corporation, with its implication that the debtor may lose its equity in the stocks of the Salt Lake and Salt Lake Western, can hardly be regarded as a desirable part of the committee's plan from the standpoint of the present bondholders.

In our prior report we stated that a consolidation of the Denver, the Salt Lake Western, the Salt Lake, the Junction, and the Goshen Valley would be in accord with our findings in *Consolidation of*

Railroads, 159 I. C. C. 522, and that it would eliminate unnecessary separate corporations and would effect operating economies. We found that such consolidation would be in the public interest and that it should be effected in connection with the plan, notwithstanding the facts that the Salt Lake, the Junction, and the Goshen Valley are not in trusteeship and that none of the corporations has sought consolidation under section 5 (4) of the Interstate Commerce Act, as amended.

The Moffat Tunnel Commission and the Tunnel District point out in their reply brief that the tunnel project was associated with the policy of the Denver to establish a new short route between Denver and Salt Lake City, that the Salt Lake became the lessee of the tunnel, and that we authorized the building of the cut-off (*Denver & S. L. W. R. Co. Construction*, 154 I. C. C. 51 and 175 I. C. C. 535) and the acquisition of control of the Salt Lake by the Denver (*Denver & S. L. Ry. Co. Control*, 170 I. C. C. 4 and 175 I. C. C. 542). A loan from the Finance Corporation for the purpose of constructing the cut-off was approved by division 4 in *Denver & R. G. W. R. Co. Reconstruction Loan*, 187 I. C. C. 399, and a loan for the purchase of the Salt Lake's stock was approved by division 4 in *Denver & S. L. W. R. Co. Reconstruction Loan*, 202 I. C. C. 489. The terms of the trackage agreement by which the Denver operates over the Salt Lake were approved in 175 I. C. C. 535, *supra*. Under this arrangement one-half of the tunnel rental is paid by the Denver. Our approval of the present relationships of the Denver, the Salt Lake, and the Salt Lake Western was predicated throughout on considerations of public interest. In particular, our finding that the public convenience and necessity required the construction of the cut-off was based upon the making of an arrangement whereby the Denver could operate on fair and equitable terms over the cut-off and the Salt Lake, thus avoiding operation of the cut-off by the Salt Lake more or less in competition with the Denver's own route into Denver. After extended negotiations this arrangement was effected. Clearly the group's modified plan, which would jeopardize the continued unified operation of these properties, is inconsistent with our heretofore-expressed policy with respect to such operation.

To upset the present financial and operating arrangements, affecting all the affiliated carriers, as well as the Moffat tunnel interests, would clearly tend to undo much of what has been accomplished towards unification. It would, in our opinion, further complicate the present difficult situation and cause great delay in the permanent improvement of the conditions under which this through route is operated. It raises the question of good faith to

the Finance Corporation, whose loans were not made in contemplation of separate operation of the properties, notwithstanding the showing of independent value for the Salt Lake. Also, to continue the present lease arrangement, if the Denver were reorganized without a consolidation, would be unacceptable to the principal interests involved and would likewise postpone the desired unification. Consolidation appears to be inevitable, and it is desirable that the necessary adjustments of the classes of creditors accompanying the reorganization of the Denver, and the consolidation, be worked out as a single transaction.

While we recognize the fact that the acceptance of the plan in the manner provided in section 77 (e) is a prerequisite to the voluntary acts necessary to effect a consolidation of the Salt Lake with the Denver, as it is to the effectuation of the plan as a whole, our first duty is to promulgate a plan which we consider both financially sound and compatible with the public interest, and we reaffirm the finding that the properties should be consolidated in connection with this reorganization.

In addition to describing its new plan for a reorganization without consolidation, the committee presented a complete draft of the provisions for the new mortgages, bonds, stock, capital fund, etc., differing both from those originally advocated by the committee and from those adopted by us.

As has been stated, the view is advanced by several interveners that the consolidation of properties proposed to be accomplished under our approved plan would be at the expense of an unduly liberal treatment of the Finance Corporation, to the injury of the Denver's bondholders. The plan provided that the Finance Corporation should receive new first-mortgage bonds in an amount equal to its principal claim, plus interest accrued to June 30, 1938, a total of $11,959,469, conditioned upon a commitment by the Finance Corporation to purchase, at par, approximately $11,443,675 of the same series of bonds, the proceeds to be used for the purpose of redeeming $11,234,000 of Salt Lake bonds outstanding, and further to purchase approximately $6,000,000 of additional bonds for the purpose of paying the debtor's trustees' certificates outstanding, the expenses of the reorganization, and for working capital. We stated that the new first-mortgage bonds probably would not be salable at par and that the Finance Corporation should be compensated in some manner for its acceptance of them at par in return for furnishing the $17,443,675 of cash necessary to carry out the plan, but that such compensation should not be limited to the probable present deficiency in the market value of

the bonds. We pointed out that from 6 months to a year probably will elapse after the Finance Corporation makes its commitment before it will be called upon to supply the funds mentioned.

The plan provides that the Finance Corporation is to receive first-mortgage bonds in settlement of its claim while the holders of the R. G. Western first trusts and the Junction first-mortgage bonds are assigned income bonds, although, according to the earnings formula, the interest requirements on these three classes of obligations are fully covered. The basis for the allotting of first-mortgage bonds to the Finance Corporation is furnished, as has been indicated, by the consideration that the Finance Corporation will advance $17,443,675 in cash, for a like amount of the new first-mortgage bonds in order that the reorganization and consolidation may be effected. The new first-mortgage bonds may not be marketable when issued at a price much above 75, in which case the Finance Corporation should be compensated in some form for a service in effect costing approximately $4,400,000. That the allotment of first-mortgage bonds in lieu of income bonds is not unduly compensatory seems evident when the probable difference in realizable value between the two classes of new bonds is considered. In our opinion the differential between their initial market prices will not exceed 30 points, or about $4,000,000 for the $11,959,469 of bonds, representing the probable maximum amount of the concession made to the Finance Corporation in respect of the qualitative treatment accorded to it. While only approximate estimates can be made in this connection, we think that our provision for the Finance Corporation is entirely justified by the circumstances. In the matter of the collateral security for the loans, we think that the element of strategic value in the stocks of the Salt Lake and Salt Lake Western is such as to outweigh any question of inadequacy of collateral on an ordinary appraisal basis.

The debtor requests us to approve the plan originally presented by it, or at least to modify our approved plan so as to provide for two classes of new common stock, to exclude interest accrued but unearned since the filing of the petition, under section 77, to increase the amount of new first-mortgage bonds issued in the reorganization, and to recognize an equity for the present stockholders. The trustee of the R. G. Western first-trust mortgage and the Junction first-mortgage contend that these mortgages should be left undisturbed and the bonds extended, or, in the alternative, that these bonds be treated not less favorably than the committee proposes in its position, or that we refuse to approve any plan at this time. The trustee of the D. & R. G. consolidated mortgage requests that we modify the plan by allotting to the holders of the

consolidated-mortgage bonds new first-mortgage bonds to an extent commensurate with the value of the mortgage property, such bonds to bear interest corresponding to the earnings of that property. The trustee of the R. G. Western consolidated mortgage urges the adoption of a 2-percent interest rate for the use of equipment, an assignment of certain equipment to the liens of the mortgages in a manner differing from that reflected in our plan, and a different disposition of the stock of the Utah Fuel Company. The trustee of the debtor's general mortgage asserts, among other things, that the holders of general-mortgage bonds should receive 1 share of new common stock for each $100 of claim, including fixed interest accrued to December 31, 1939 (18 months later than the effective date of the plan), together with one-half share for each $100 of contingent interest accrued between February 1, 1924, and February 1, 1929, making a total of 430,974 shares of new common stock, as compared with 123,786 shares allotted to these bondholders in the plan.

The Chase National Bank of the City of New York, as noteholder, contends that the 10-year extension of its note, subject to renewal at the option of the new company, for further periods of 10 years each, as provided in the approved plan, is inequitable, and, inasmuch as the present note is a demand note and became due and payable when the petition under section 77 was filed, the renewal should be for 10 years only. The trustee of the Missouri Pacific Railroad Company urges that our plan provide for the retention by that carrier of its half interest in the Denver, as a matter of public interest, regardless of the existence of any equity for the Denver's present stock. The trustee also questions our provision that the new preferred stock shall have voting rights, since the present preferred is without such rights, and suggests that either the new preferred should not have voting rights equal to the common or it should be permitted to elect only a minority of the board of directors. The Security Research Bureau suggests numerous revisions of our plan, including an increase in fixed charges, the addition of a prior-preferred stock, changes in the mortgage and stock provisions, changes in the formula calculations and the allotment of new securities, and a different treatment of the claims of the Finance Corporation. The petitioners criticized practically every feature of the plan. We shall not undertake here to review in detail the contentions made with respect to the various points at issue, nearly all of which were discussed in our prior report.

After consideration of the petitions, briefs, and reply briefs filed, we conclude that the proceeding should not be reopened for further hearing or oral argument, that the suggested reorganization with-

out consolidation would be inconsistent with the record made herein and contrary to the public interest, and that as to all essential matters the petitions should be denied.

From a reconsideration of our prior report and order, we are of the opinion that certain provisions of the plan should be modified and certain other provisions, as to which some question has been raised, should be retained without change. These matters are discussed below and our conclusions are stated.

New First Mortgage

1. In the plan formerly approved it was provided that the interest on the first-mortgage bonds issued in the reorganization should be payable annually. In order to conform with usual practice and to enhance the marketability of the bonds, we conclude that this provision should be revised so that the fixed interest shall be payable semiannually.

2. Our plan provided that no additional first-mortgage bonds should be issuable unless the income of the new company available for fixed charges in a period of 12 consecutive calendar months within the preceding 18 calendar months equals or exceeds 1½ times fixed charges. Believing that this requirement is unduly restrictive and in general ineffective, we conclude that the provision should be omitted in the plan. See *Chicago, M., St. P. & P. R. Co. Reorganization*, 239 I. C. C. 485.

3. The provision for a special sinking fund for the retiral of first-mortgage bonds when the amount of fixed-interest debt exceeds a certain percent of total capitalization is retained. Those provisions would be effective when the total principal amount of fixed-interest-bearing securities exceeds 35 percent of the total capitalization, or 50 percent of the total capitalization less the amount of contingent-interest-bearing debt. The committee asks that these two percentages be increased to 50 and 60, respectively. Under the capitalization and initial debt provided for in our plan, the second of these criteria would, within all practical limits, constitute the limitation on the issue of new fixed debt as long as the contingent-interest debt remains the same. The criterion of 50 percent proposed by the committee would be ineffective under such circumstances. In our opinion the 35 percent approved by us should not be modified.

It appears that the second criterion approved by us is susceptible of two interpretations, and under one interpretation would force the immediate use of the sinking fund. The 60-percent limitation proposed by the committee would, under this interpretation, per-

mit the issue of approximately $30,000,000 of first-mortgage bonds, and we approve that limitation.

In order to avoid possible ambiguity in the language of our former report and also to make the above-indicated adjustment, the following is approved as a modification of the opening sentence of the provision in question:

(2) When on any interest payment date the aggregate principal amount of first mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either 35 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the mortgage trustee as a sinking fund a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, the payment to the capital fund, contingent interest, and sinking fund payments for the retirement of income bonds as hereinafter prescribed.

No further changes in the provision for this sinking fund are necessary.

4. The following additional provision regarding the pledging of first-mortgage bonds as collateral is approved:

The first mortgage shall contain a covenant substantially to the effect that the excess of the aggregate amount of all first-mortgage bonds under pledge at any one time, over the principal amount of all indebtedness so secured, shall not exceed 10 percent of the aggregate principal amount of all first-mortgage bonds then authenticated and uncanceled.

5. The following provision, being superfluous, is deleted from the plan:

No sinking funds shall be provided for the new first-mortgage bonds (except in the case of bonds issued for equipment) other than as provided in (2) above.

New Income Mortgage

The following additional provision regarding the pledging of income bonds as collateral is approved:

The income mortgage shall contain a covenant substantially to the effect that the excess of the aggregate principal amount of all income-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured shall not exceed 10 percent of the aggregate principal amount of all income-mortgage bonds then authenticated and uncanceled.

Application of Available Net Income

The following provision is approved as a substitute for paragraph 3 in the sequence in the approved plan describing the application of available net income, in order to give effect to the special sinking fund for the retiral of new first-mortgage bonds:

3. Any then remaining available net income shall be applied to payment to the sinking fund to be created and paid to the trustee under the first mortgage in the event the principal amount of first mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either (*a*) 35 percent of the total capitalization of the new company, determined as elsewhere provided in the plan, or (*b*) the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding.

New Preferred Stock

The meaning of the closing sentence of the provisions for the new preferred stock being questioned, we approve the following in lieu thereof:

The new preferred stock shall be convertible at the option of the holder at any time, except that stock which is called for redemption shall be convertible not later than 15 days prior to the date as of which such call shall be made, into new common stock at the rate of one share of common stock for each share of preferred stock.

Chase National Bank Note

We approve a revision of the provision for extending the debtor's obligation to this bank so that the new note or notes shall mature in 10 years, without an option to the new company to extend the note or notes. The opening sentence of our provisions for the note will be modified to read as follows:

The secured note held by the Chase National Bank shall be canceled, and a new note or notes issued in face amount equal to that of the present note, plus interest accrued to June 30, 1938, in the amount allowed by the court, such notes to mature in 10 years and to bear interest at the rate of 4 percent per annum, payable semi-annually on October 1 and April 1 of each year, but such interest shall be contingent on, and payment thereof shall be limited to, the total of the interest and dividends paid by the new company on the collateral securing such notes.

No further changes in the provisions for this bank note are approved.

In the summary of the approved plan, 233 I. C. C. 515, 593, the annual interest on the extended note was shown as a fixed interest charge. In the revised summary of plan, shown later herein, such interest is included as a contingent charge.

Adjustment of Amounts of Claims

The adoption of the following new provision in the plan is approved:

In view of possible changes in the amounts of the obligations shown as outstanding, the reorganization committee shall be authorized, in order to give

effect to such changes, to make such adjustments in the claims provided for in the plan, and such changes in allotment of securities, consistent with the provisions of the plan, as may be approved by the court.

Voting Trust

Our prior report and order provided for the creation of a voting trust for the new common stock for the primary purpose, as explained in the report, of permitting a sale of control to the present proprietary companies or others, as the stockholders might decide, the terms and conditions of such sale to be subject to our approval. Upon further consideration we deem it desirable that both the new preferred and the new common stock be deposited under the escrow agreement, since the two classes of new stock are to have the same voting rights. With this modification and a provision for the compensation and expenses of the trustees, the approved provisions for the voting trust will read in full as follows:

K. All the preferred stock and common stock issued by the new company in the reorganization, excepting shares issued to qualify directors, shall be deposited under an escrow agreement with a bank or trust company designated by the court, and escrow receipts issued to the persons entitled to receive such stock under the plan. The escrow agreement shall be for a term of 10 years from the date of creation of the trust, but not later than 6 months after confirmation of the plan, and shall provide that the reorganization committee, as voting trustees, may, subject to the approval of this Commission, and with the consent of the holders of escrow receipts representing not less than a majority of the shares of preferred stock on deposit, sell all or any part of such deposited preferred stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders; likewise the voting trustees may sell all or any part of the deposited common stock with the consent of the holders of escrow receipts representing not less than a majority of the shares of common stock on deposit. It shall be provided that all holders of escrow receipts shall be bound by the terms of any sale or sales which shall have been approved by this Commission and consented to as aforesaid, and the net proceeds of any sale or sales, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts for preferred stock and common stock, respectively, according to the class of stock sold. During the life of the escrow agreement, the holders of escrow receipts shall have the right to receive notice of all meetings of stockholders and to direct the voting trustees as to the manner in which the stock represented by the escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stock shall be voted in such manner as the voting trustees may determine. The reasonable compensation and expenses of the voting trustees, including counsel fees, shall be paid by the new company.

Unsecured Claims

The record showed that the amount of general unsecured claims outstanding was approximately $440,000, of which an undetermined amount fell within the 6-month rule. The unpledged securi-

ties owned by the debtor and its subsidiaries having a realizable value consisted of $46,000 of certificates issued by the receiver of the Rio Grande Southern Railroad Company and $850,000 of United States Treasury bonds. The latter have passed out of the debtor's possession. The present value of the receiver's certificates is uncertain, but in any event any distribution of new stock based upon this free asset, among the holders of the general claims and among the holders of the general-mortgage bonds in recognition of claims which they might present based upon the allotment of new common stock under our plan, would obviously be insignificant in amount. We conclude that the equity of the holders of unsecured claims not entitled to priority is without value and that these creditors should not be permitted to participate in the plan. Our modified order will accordingly omit provision for the general unsecured claims.

Reorganization Committee

Our plan provided for a reorganization committee to consist of five members, two to be designated by the insurance-group committee, as representing the R. G. Western mortgages, the Junction first mortgage, and the D. & R. G. consolidated mortgage, one member to be designated by the trustee under the debtor's refunding and improvement mortgage, one by the trustee under the debtor's mortgage, and one by the Finance Corporation. Further consideration of the composition of the committee has not resulted in any change in our views regarding it. Under our plan the Finance Corporation will have a large interest in the new company, and we think that it is clearly entitled to representation on the committee.

The two following revisions of the provisions for this committee are approved:

[new] Should any of the parties named fail to designate its representative or representatives, as the case may be, within such time as the court shall consider reasonable, the court shall appoint such representative or representatives.

[modified] The members of the committee, as such, shall agree to serve without compensation, but the expenses of the committee shall be paid by the new company, subject to the provisions of section 77 and the approval of the court, as part of the cost of effectuation of the plan. In their capacity as voting trustees the members of the committee shall be entitled to compensation and expenses as provided above in connection with the voting trust.

* * * * * *

Allocation of new securities under plan disapproved by the court omitted here.

We conclude that except as herein indicated the requests for modification of the plan of July 11, 1939, should be denied. An appropriate order will be entered accordingly, in which, with the foregoing modifications, our former plan will be approved. Such order will supersede the order of July 11, 1939.

EASTMAN, *Chairman*, concurring in part:

The essential purpose of the bankruptcy proceeding is to protect the interests of the creditors of the Denver, and the reorganization plan ought to make the best possible provision for them that the circumstances will permit. I am not wholly persuaded that consolidation of the Denver with the Salt Lake and the Salt Lake Western on the terms proposed will accomplish this result. It seems to be assumed that large benefits will accrue to the Denver from such a consolidation and that these benefits will be lost if the properties should become independent in ownership and operation. It is not clear to me that this assumption is correct, and I should be glad to hear argument on the point.

As between the Denver and the Salt Lake, my impression is that the Denver has the advantage in strategic position. The connection between the two railroads via the Dotsero cut-off is of value to both, but it would seem that it is more valuable to the Salt Lake than to the Denver. The latter now constitutes the only outlet of the Salt Lake to the west, but the Salt Lake does not constitute the only outlet of the Denver to the east. It has quite a good outlet for most eastern traffic via Pueblo and the Missouri Pacific. If the Salt Lake and the Salt Lake Western were independently owned, it seems to me that the Denver could safely rely upon this strategic position for assurance that favorable traffic and operating arrangements via the cut-off route could readily be made, and that the possibility of a unification of the roads on terms fully as favorable as, and probably more favorable than, those now proposed would not at all be foreclosed. This assurance would be strengthened by the natural interest of the Burlington, and to some extent of the Rock Island, in the development of the cut-off route.

Much is said in the report about our prior approval of the present relationships of the Denver, the Salt Lake, and the Salt Lake Western, and about "good faith to the Finance Corporation, whose loans were not made in contemplation of separate operation of the properties." As it happens, I did not join in the approval of acquisition by the Denver of stock control of the Salt Lake at the price of $155 per share, and believe that this transaction was harmful rather than helpful to the Denver; but, however that may be, the interests of the creditors of the Denver are paramount in the pres-

ent proceeding, if I understand the law correctly. And it seems to me that the Finance Corporation, when it made the loans in question, assumed the customary risks of such transactions.

I record these impressions for what they may be worth. It may be that they are wrong, but as at present advised I cannot join in what is said in the report with respect to the consolidation of these properties.

COMMISSIONERS MAHAFFIE and PATTERSON did not participate in the disposition of this case.

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Text of plan disapproved by the court omitted here.

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted March 5, 1942. Decided July 13, 1942

Upon record previously made, the record made in proceedings before the court, and further hearing, the plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, further modified and approved.[1]

Appearances as in prior reports, and also *Montgomery Dorsey, William J. Kane, Emmet McCaffery, Russell L. Snodgrass, Guy M. Springer, Jr.*, and *W. Brua Campbell.*

Second Supplemental Report of the Commission

BY THE COMMISSION:

Exceptions to the examiner's second proposed report were filed, and oral argument was heard. Our conclusions differ from those of the examiner.

The abbreviated titles of companies used in our prior reports will be followed herein. The insurance group committee will be referred to as the committee, and the Reconstruction Finance Corporation as the Finance Corporation.

Status of the proceedings.—By our report and order of July 11, 1939, in this proceeding, 233 I. C. C. 515, we approved a plan of reorganization of the debtor and the secondary debtor, and by a supplemental report and order, dated April 2, 1940, 239 I. C. C. 583, we approved a modified plan. The modified plan was duly certified to the District Court of the United States for the District of Colorado, where the proceedings for reorganization are pending. Pursuant to an order of that court entered May 6, 1940, objections to the plan were filed with the court by the debtor, the committee, the Finance Corporation, and other parties, and the case came on for hearing on July 29, 1940. Following an informal conference

[1] Previous reports: 212 I. C. C. 105 and 709; 217 I. C. C. 101; 224 I. C. C. 574; 233 I. C. C. 515; 239 I. C. C. 583; and 242 I. C. C. 529 and 721.

with the parties after the close of the hearing, the judge issued an interim memorandum, dated August 30, 1940, in which he expressed his views regarding the main features of the plan. Further conferences were held; and a new plan, proposed by the committee and known as the discussion plan, was considered. On December 6, 1940, the judge filed an opinion in which he criticized the discussion plan and our modified plan, and suggested a different plan.

The adoption of the discussion plan was urged in a petition filed with the court by the Central Hanover Bank & Trust Company, trustee of the Rio Grande Western first-trust mortgage. On January 6–8, 1941, the court heard the parties in oral argument, after which several conferences were held. A plan referred to as the FitzGibbon plan was presented at these conferences. On March 7, 1941, the court entered an order overruling a motion to dismiss the proceedings, disapproving our modified plan, and referring the proceedings back to us, with an opinion dated March 6, 1941. In this opinion, the judge indicated his objections to the various plans offered, including a plan proposed by the Finance Corporation, and described a plan which he recommends, hereinafter referred to as the court plan. The record made in the court proceedings was transmitted to us, and has been considered by us as a part of the record in the proceedings.[2]

Upon petition by the committee, an order was entered reopening the proceeding and assigning it for further hearing on May 20, 1941, for the purpose of receiving evidence to bring the record of the debtor's operations down to date, and such other evidence and suggestions as would assist in a reconsideration of the plan. Briefs were filed. The briefs were devoted largely to criticisms of, and suggested changes in, the court plan. In connection with its exceptions to the examiner's second proposed report, the committee suggested various changes in the plan therein recommended, embodying such suggestions in the form of a new plan.

The court plan.—The court plan differs in essential respects from our modified plan of April 2, 1940, although intended to be within the framework of the latter. The court agreed with us regarding a consolidation of the lines, stating in its opinion that, "Consider-

[2] Section 77, subsection (c), provides in part as follows: "If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) hereof."

ing the public's point of view and that of all creditors, this particular situation requires a consolidation of the Rio Grande and the Denver & Salt Lake." But the court's provision for consolidation was that it would be effected only in the event the holders of at least 66⅔ percent of the Salt Lake income bonds voluntarily accept a modification of the interest provisions of these bonds so that they would bear fixed interest at 4 percent. The effective date of the court plan would be January 1, 1941, while that of our modified plan was June 30, 1938, involving an increase of approximately $15,000,000 in accrued interest on funded debt, together with new equipment obligations. The amount of new first-mortgage bonds would be increased from $29,403,144 of 4-percent bonds, as provided in our plan, to $41,120,142 of bonds bearing 3-percent fixed interest and 1-percent prior-contingent interest. The $1,278,539 of annual fixed charges in our plan would be increased to $1,887,552 under the court plan, principally by the inclusion of the Salt Lake bonds. The allocation of securities to others than the Finance Corporation was generally on the same percentage basis as in our plan, but, as a consequence of the increase in first-mortgage bonds and the different treatment of the claim of the Finance Corporation, the court's treatment of the Denver's bonds was much more favorable. The court plan provides that the payment to the capital fund, a maximum of $750,000 per annum, be made prior to the payment of fixed interest, rather than immediately following. For the new money required in the reorganization, the Finance Corporation was asked to purchase $6,000,000 of income bonds, which would be convertible as a unit into class B common stock, carrying sole voting power. The right of sale of this stock by the Finance Corporation, for its reimbursement, would be restricted so that no one of the connecting railroads could obtain more than 40 percent thereof.

In our report of April 2, 1940, *supra*, we reviewed the development of the cut-off route, the close affiliation between the component roads, the Moffat tunnel interest, and the question of public interest, and reaffirmed our previous finding that the properties should be consolidated in connection with this reorganization. We also pointed out the status of the Finance Corporation as pledgee of the stocks of the Salt Lake and Salt Lake Western, and stated our reasons for the treatment accorded the claims of the Finance Corporation. It appears that the court rejected our modified plan because, through this treatment of the Finance Corporation and the relative treatment of the debtor's bondholders, particularly those owning the bonds of the Rio Grande Western and the Junction, the price to be paid for consolidation was too high, and the

plan was deemed inequitable. It is apparent that in this important respect our former plan is impossible of approval or acceptance.

The most feasible means of effecting a consolidation of the Salt Lake now appears to be along the lines suggested by the court. As to the court's treatment of individual claims, we are unable to accept the view expressed by counsel for the committee, that the court plan constitutes an adjudication of the rights of the creditors and is now the law in the case. We do not think that the court intended to preclude us from preparing and approving a new plan, provided such new plan reflects the equitable principles laid down in its decision.[3] Full consideration has been given by us to the conclusions and suggestions of the court, and in the light of them and from our review of the evidence we have made the determinations as to the treatment of creditors, hereinafter set forth.

Debtor's position.—Despite our finding that the equities of the debtor's stockholders have no value, and the court's failure to find otherwise, the debtor still contends that an equity worth at least $40,000,000 exists, that no reorganization can be accomplished without a lawfully determined valuation of the property, and that the fairness of the court plan cannot be determined without such valuation. However, various specific objections to the court plan were offered, such as its recognition of interest accruals in excess of $7,000,000 since September 1, 1935, the treatment of the Finance Corporation, the provisions for sale of control, and the inclusion of the Junction, which is not a debtor under section 77. The debtor—

> reserves its objections to the proceedings going forward before the Commission or the court until a new plan or plans are filed, the feasibility thereof determined, and hearings thereon ordered in accordance with subsection (d) of section 77 of the Bankruptcy Act.

The debtor's general position with respect to the purpose and scope of section 77, and the rights of creditors and stockholders, was stated in 233 I. C. C. 515, *supra*, at pages 573 and 578, and requires no further comment. Since our previous decision in this case, the decision of the United States Supreme Court in the case of *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, sup-

[3] In this connection the court said: "My three opinions in this matter, it is thought, set forth the reasons moving the Court to disapprove the ICC Plan and send it back to the Commission for further hearings and consideration. The Court recognizes the Commission is well versed and peculiarly fitted to appraise the values of different interests and the soundness and fairness of any plan. If it does not agree with the views of this Court, any new plan they submit is most likely to receive our approval. The rights of the parties have been so minutely explored and discussed that it is hoped there may be little difficulty in the parties reaching an agreement upon a plan that meets the views of the Commission and the Court which are now in the record."

ports the views expressed by us with respect to the treatment of accruals of interest, and our disposition of the rights of the stockholders.

The plan herein approved, for reasons which will be stated, differs materially from the court plan and from the plan previously approved by us. In our opinion, the procedural requirements of section 77 have been and are being followed by our action in immediately hearing objections to the plan suggested by the court, without delaying the proceedings 6 months or more pending the filing of new plans for our consideration. We hereinafter specifically find the value of the properties for the purposes of this proceeding.

Consolidation of the properties.—The modified plan herein approved provides for the merger or consolidation of the properties of the debtor, the secondary debtor, the Junction, the Goshen Valley, and the Salt Lake; that of the secondary debtor to take place only if the Salt Lake is merged or consolidated, which would be subject to acceptance by the holders of the Salt Lake income bonds of the proposal for modification of the interest terms and maturity thereof, as hereinafter described. The manner of effecting such merger or consolidation should be determined by the reorganization committee, subject to approval by the court, and under a fair and equitable arrangement to protect the interest of the railroad employees affected, as required by law.

The present plan specifies the treatment accorded to each class of claims on the basis of consolidation with the Salt Lake, with appropriate provisions for the claims in the event such consolidation is not accomplished. If the consolidation becomes effective, the contract for use of the Moffat tunnel should be assumed by the new company, the holders of Salt Lake stock outstanding in the hands of the public should receive new securities in exchange therefor, and the payment of interest on both classes of Salt Lake bonds, modified so far as the income bonds are concerned, as provided in the plan, should be assumed by the new company, all as hereinafter set forth. The bonds of the new company should be secured by the combined properties of all the roads, subject to the prior liens of the Salt Lake mortgages with respect to the Salt Lake properties.

In the event the holders of the required percent of Salt Lake income bonds do not assent to the proposed modification of their bonds, and the consolidation thereby fails, the separate operation of the Salt Lake would continue and the stock outstanding, as well as the first-mortgage bonds and income bonds, would remain un-

disturbed. In this situation, the mortgage bonds of the new company would be secured by the properties of the debtor, the Junction, and the Goshen Valley only.

In neither event would the Salt Lake bonds be affected as to their liens.

Earnings; equity.—In our report, 233 I. C. C. 515, *supra*, at pages 551–552, we discussed the earnings record of the carriers, and showed that the lowest system income available for interest in the last decade was in the 3-year period 1936–38. After adjustment for extraordinary expenditures for deferred maintenance, the average annual income available was stated at about $2,893,255. The total of the fixed-interest charges approved under our modified plan and the maximum annual payment to the capital fund was approximately $2,098,536, which would have been covered 1.38 times by the foregoing amount of adjusted income. We stated, at page 552, that:

> In giving this consideration to the low earnings of recent years our position is not that the system lines will never regain their former earning power, or exceed it, but rather that, with the present conditions in the railroad field and in the public interest, a conservative policy should be followed * * *.

The evidence adduced at the further hearing shows that the improvement program has been substantially completed. From the appointment of the debtor's trustees on November 1, 1935, to March 31, 1941, a total of $22,916,051 was expended on the debtor's property, of which $17,504,246 was chargeable to capital account. The ratios of maintenance to total revenues had been 35.12 in 1935, 41.09 in 1936, 46.83 in 1937, and 39.09 in 1938. The debtor believes that the improvements already made, together with the acquisition of new Diesel switch engines and road engines costing $4,000,000, will produce a large and permanent reduction in operating costs. The results of operation in 1940 are considered by the committee to be fairly representative as to economy of operation as well as to gross revenue, based on 5 years of the trusteeship. The income of the Denver available for interest in 1940 was shown as $2,800,514[4] and the Salt Lake's available income as $509,771, a total of $3,310,285. Previous totals were $2,299,867 in 1939, $673,358 in 1938, $295,504 in 1937, and $2,327,757 in 1936. The committee pointed out that, applying the unit costs of operation in 1940, the available income of the combined roads would have been $3,288,501 in 1939, $2,970,135 in 1938, $3,774,334 in 1937, and $3,890,570 in 1936. The average for the 5 years would have been $3,446,765. These

[4] Adjusted from the amount of $2,647,086 shown in the 1940 annual report of the Denver's trustees to the stockholders.

figures reflect operating charges of approximately $1,000,000 a year in connection with improvements. The forecast for 1941 indicated an available income of $3,513,590 for the combined roads, and the actual amount was $5,019,436.

We cannot, of course, accept the committee's adjusted figures as expressing what the company's earnings would have been under improved conditions in the stated years. The earnings in 1940 and 1941 indicate an improvement in the earning power of the system, but do not justify a modification of our findings regarding the equity of the Denver's stockholders (233 I. C. C. 515, at page 580) or of the holders of unsecured claims (239 I. C. C. 583, at page 594). The principal of the debt (including R. C. C. notes, R. F. C. notes, and trustees' certificates), of the Denver as of January 1, 1942, is $143,181,421, and annual interest charges thereon amount to $6,137,715. In addition, accrued and unpaid interest to January 1, 1942, on the Denver's debt amounts to approximately $42,499,558, and interest on this obligation at the rates applicable to the principal obligations would require an additional $1,944,555. The claim on this unpaid interest must also be provided for before the junior claims and the stock can receive anything. Interest upon the principal and unpaid interest of the Denver's debt at 4 percent is $7,427,239 and at 5 percent is $9,284,049. Both amounts exceed the above-stated income available for interest in either 1940 or 1941 for the Denver or the Denver and the Salt Lake combined. Income of the Denver and the Salt Lake available for interest in 1940 capitalized at 4 percent is $82,757,125, and capitalized at 5 percent is $66,205,700, and the above-stated system earnings for 1941 similarly capitalized are $125,485,900 and $100,388,720, respectively. Each of these amounts is less than the principal amount of the Denver's debt. We reaffirm our findings that the equities of the owners of the debtor's common stock and preferred stock have no value and that the holders of claims in classes 1 and 2 are not entitled to participate in the plan; and that the equity of the holders of unsecured claims not entitled to priority is without value and that these creditors should not be permitted to participate in the plan.

New capital structure, fixed charges.—Under the court plan, the total capitalization of the new consolidated company, taking the common stock at $100 a share, would be $161,611,891, the total debt would be $90,411,051, and the total charges before dividends $4,569,644. Fixed charges would amount to $1,887,552 per annum, without the capital fund, and $2,637,552 per annum, including the payment of $750,000 to the capital fund, which the court placed

ahead of all fixed interest. There would be a further increase of $411,201 if the court plan were modified as suggested by the committee so as to make the prior contingent interest on the new first-mortgage bonds a fixed charge in the event all fixed and prior contingent interest should be earned 1½ times in each of 3 calendar years in any 5 consecutive years, such 3 years to include the last 2 of each 5 years. The court had before it, in addition to the record made before us, the results of operation for the years 1939 and 1940.

In determining the amount of fixed charges in connection with our former plan, we gave consideration, as above stated, to the carriers' earnings record up to the close of 1938, including the low earnings during 1936–38 as actually reported, and as adjusted for deferred maintenance. The total amount of fixed-interest charges which we approved for the consolidated company was approximately $1,278,539, not including the capital-fund requirement. The development of the record at the further hearing before us led the examiner to recommend a limit of approximately $2,000,000. The total fixed-interest charges under the plan hereinafter approved are shown as $1,766,966, on the basis of the present equipment obligations and a consolidation of the properties.

The improvements recently completed on track and structures, together with the new acquisitions of equipment, will undoubtedly result in more efficient operation and reduced cost of maintenance. The committee concludes from its studies that the minimum future earning capacity of the combined properties is substantially in excess of $3,000,000 a year, and the court has expressed a similar opinion. In view of the record of the results of the debtor's past operations, as hereinbefore set out, the emphasis which the court has placed on measures to prevent future financial difficulties, and the uncertainty of future economic conditions in the country, and considering all of the facts of record with respect to the debtor's earning power, and all other relevant facts, we find that the total fixed-interest charges under the plan herein approved, on the basis of the present equipment obligations and a consolidation of the cut-off lines with the Denver, should not exceed approximately $1,766,966. Further, we believe that the plan should provide that payment of the fixed interest on the new first-mortgage bonds may be deferred, with the assent of the bondholders, under the conditions and in the manner hereinafter stated.

For the purpose of comparison with our former plan, the above amount plus the payment of $750,000 to the capital fund equals $2,516,966. This amount was covered 1.37 times by the average earnings during the period 1936–40, developed by the committee

on the basis of 1940 operation costs. Under the former plan, the corresponding charges were covered 1.38 times by the adjusted earnings of 1936–38. We find that, under the conditions imposed, the above charges will be adequately covered by the prospective earnings of the reorganized company.

Effective date.—The effective date of the plan recommended by the examiner, and shown in the modified plan suggested by the committee, was January 1, 1942, 1 year later than the date of the court plan. It is clear that a date later than that of the court plan should be adopted. We have considered the cash position of the debtor, its recent earnings record, the probable payments of interest and other probable disbursements by the trustees during 1942, and the cash requirements for interest payments and other payments, in order to carry out the plan herein approved. The system cash on hand January 1, 1942, amounted to $4,886,345, which, added to the cash receipts during 1942, as estimated from operations in the first 3 months, and giving effect to the proposed loan of $2,250,000 for new money, amounts to approximately $15,575,345. The total cash disbursements during 1942 under the plan would be approximately $12,231,000, including the payment of all outstanding trustees' certificates. The result of these estimates shows at least $3,344,000 of cash on hand at the close of the year. According to the testimony of the debtor's witnesses, this amount will be ample for cash working capital. Despite the increase in the total of present claims between January 1, 1941, and January 1, 1942, we conclude that the latter should be adopted as the effective date of the plan.

Capital fund.—We are reluctant to set aside the suggestion of the court that the payments into the capital fund be required or permitted prior to payment of fixed interest, but it seems desirable to avoid detracting from the future market value of the new first-mortgage bonds by appearing to provide for nonpayments of the fixed interest on them as a matter of course. Obviously, such a provision would be used or useful only if the earnings should be insufficient to make both the fixed-interest and the capital-fund payments. The virtual completion of the debtor's improvement program also tends to lessen the necessity for giving precedence to the capital-fund payments. The capital structure hereinafter approved by us is such that there are reasonable prospects in most years of making the capital-fund payments out of earnings, after payment of fixed-interest charges. We conclude that the payments into the capital fund should not be required or permitted prior to the payment of fixed interest.

Equipment fund.—The court also urged that the annual depreciation charge on equipment should be set aside in a special cash fund and used only to take care of interest and principal payments on equipment-trust obligations outstanding or issued later, and to take care of, in whole or in part, the purchase, building or improvement of equipment. The plan herein approved imposes strict limitations upon the reorganized company with respect to the use of its cash. The provisions of the mortgages prescribe the purposes for which all funds remaining after charges for operating expenses, including depreciation, may be used. At present, the maturities of the debtor's equipment obligations will require approximately 85 percent of the accruing depreciation reserve. This condition will continue for at least 7 or 8 years. In view of the foregoing, it is our view that we should not impose the suggested limitation of the use of the depreciation reserve.

Property valuations.—In our report, 233 I. C. C. 515, *supra*, at pages 521–523, we stated that the report of our Bureau of Valuation showed the cost of reproduction of the system properties, less depreciation, plus lands and rights, working capital, and net additions and betterments to December 31, 1936, as $147,717,268. If to this sum be added the net changes in investment accounts, reported in the carriers' annual reports for 1937 to 1940, inclusive, the total becomes approximately $155,900,000. A substantial addition to this sum will have been made during 1941, especially from acquisitions of equipment. On the basis of original cost, as also stated in 233 I. C. C. 515, *supra*, the total as of December 31, 1936, was $178,024,641. Adding the net changes in investment for the years 1937–40, this would become $186,207,418.

The securities representing investments of the debtor may be divided into four groups, as follows:

1. Those issued by subsidiary railroad companies which will be merged or consolidated with the debtor and whose operations have been taken into account in fixing the new capitalization. These securities will be canceled upon consummation of the plan, and no determination of their value is necessary, except in connection with the claim of the Finance Corporation, hereinafter discussed.

2. Securities (excluding $906,000 of Junction refunding bonds, which fall within the foregoing category) which are now pledged under the present refunding and improvement mortgage, in whole or in part, and which will be released upon consummation of the plan and presumably become subject to the lien of the new first mortgage. These securities consist of stocks of the following terminal companies in the par amounts indicated: $5,000 of stock of the Denver Union Terminal Company, $10,150 of stock of the

Pueblo Union Depot & Railroad Company, and $100,000 of stock of the Salt Lake City Union Depot & Railroad Company. The total book value of these stocks is $115,150. The income accounts of the three companies show deficits throughout from 1927 to 1936. These deficits are paid by the lessees of the terminals, and the Denver's portion is carried into its accounts as joint facility rents or other proper account. The operation of the terminal companies, therefore, is reflected in the distribution of net earnings.

3. Miscellaneous securities, some of which will be released from pledge upon consummation of the plan, and others of which are not under pledge, which presumably will be held as free assets by the new company. These comprise the Motorway stocks and the Rio Grande Southern bonds, all hereinafter considered in connection with the Finance Corporation claim, together with 5 shares of stock of the Railway Express Agency, $50,000, par value, of the stock of the Denver Market & Produce Terminal, and $2,801, par value, of the stocks of 12 small nonaffiliated companies. The total book value of the securities, other than the stocks and bonds pledged with the Finance Corporation, is about $95,000. We find that the free assets consisting of these securities have a value not exceeding the sum just stated.

4. The stock of the Utah Fuel Company, which is pledged under the Rio Grande Western consolidated mortgage, subject to the right of redemption. The evidence as to the value of this stock was reviewed in our report 233 I. C. C. 515, *supra*. The going-concern value of the property was appraised by a mining expert in 1937 at $4,653,720, which the trustee of the mortgage considers to be a conservative figure. The company's earnings are not of record since 1936, in which year, and in 1935, small amounts of net income were reported. The debtor, in its original earnings formula, credited the Rio Grande Western consolidated-mortgage district with an income of $83,333 a year from the fuel company. In the first plan presented by the committee, the allocation of new bonds to the claim of the Rio Grande Western consolidated included an allowance of $567,448 of income bonds for control of the fuel company. Since our plan provides that the beneficial interest in the stock shall be distributed pro rata to the bondholders, the matter will be discussed later in connection with the bondholders' claim.

New capitalization.—While the debt of the Denver has increased materially since the effective date of the former plan, there has also been an increase in earning power, as we have shown. Capitalized at 4 percent, the income of the system available for interest

in 1941 produces the sum of $125,485,900, and at 5 percent it produces $100,388,720. The trend of earnings indicates that in 1942 the debtors' forecast for a future normal year, showing an available income of $6,215,423, will be exceeded. That forecast of income capitalized at 4 percent would amount to $155,385,600, and at 5 percent, $124,308,500. Considering the entire record, and taking into account the elements of value of the properties involved, their past and present earnings and prospects for future earnings, as well as other pertinent factors, we conclude and find that the value of the properties for the purposes of this proceeding is $154,521,612, and that the total capitalization upon consummation of the plan should not exceed approximately that amount.

The new capital structure and the allocation of securities which we now approve, excluding securities to be pledged, are shown in tabulated form in appendix A, based on a general consolidation of the properties and the inclusion of the Salt Lake bonds, and in appendix B, without such consolidation with modification of the interest terms of the income bonds. Under this plan, the fixed charges would approximate $1,766,966, comprising $193,832 of interest on equipment obligations, interest at 3 percent on $36,120,366 of new first-mortgage bonds, interest at 4 percent on $1,500,000 of Salt Lake first-mortgage bonds, interest at 3 percent on $9,734,000 of Salt Lake income bonds (assuming all the holders consent to the modification of interest terms), and the estimated fixed interest payments on the Chase Bank note extended, the Railroad Credit Corporation note if extended, and a loan for new money in the amount of $2,250,000. Prior contingent-interest charges on the new first-mortgage bonds, the Salt Lake income bonds, and the new first-mortgage bonds to be pledged with the Chase Bank will amount to approximately $473,494. Contingent-interest charges on the $21,916,638 of new income bonds, and on the income bonds to be pledged with the Chase Bank (up to a total of 4 percent on the amount of the new note to be given the bank), will total approximately $1,009,185.

The total debt of the new consolidated company under this plan would be approximately $82,994,255, and the total capitalization would be approximately $154,521,612, including all equipment obligations. Total charges ahead of dividends on the preferred stock, including the maximum payment to the capital fund and the sinking funds, would be approximately $4,235,039, as compared with $4,093,842 in the plan formerly approved. This increase is justified on the basis of the earnings record, as supplemented at the further hearing. We find that the amount of the new company's obligations and the annual charges above stated may not be exceeded.

The capitalization last stated included $3,927,605 of obligations for equipment acquired in 1941, consisting of 17 Diesel locomotives and 5 Mallets, purchased under conditional-sale agreements totaling $2,667,605; and 500 boxcars acquired under equipment trust I for $1,260,000. The operating savings from this new equipment are not reflected in the unit costs in 1940, which were adopted by the committee as a criterion in adjusting the income accounts of 1935–39, and, on the theory that this new equipment will pay for itself by the economies which it will produce, the $3,927,605 of new equipment obligations might properly be considered as a separate item in the capital structure, in effect reducing the new total to $150,594,007. This figure would be comparable with the total capitalization of $147,433,350 under our former plan, taking the no-par common stock at $100 a share.

The effect of a reorganization of the Denver without consolidation of the Salt Lake would, under this plan, be to eliminate from the new capital structure the $11,234,000 of Salt Lake bonds, the $411,100 of new preferred stock allocated to the shares of Salt Lake stock outstanding in the hands of the public, and $1,000,000 of the loan for new money, hereinafter discussed. Also, instead of the new securities shown in appendix A as allotted to the Finance Corporation claim, other securities would be assigned for the system securities under pledge, and these, together with the remainder of the collateral, would be deposited in escrow for the benefit and interest of the Finance Corporation, subject to prescribed conditions, as hereinafter stated. On this basis, and with the Finance Corporation claim shown at its present amount, the total capitalization of the reorganized Denver would be substantially $141,876,512, the total debt $72,351,856, total fixed interest $1,765,973, and total charges before dividends $3,732,956.

Basis of allocation of new securities.—In our report in 233 I. C. C. 515, *supra*, at page 582, certain modifications of the debtor's segregation formula were introduced, for reasons stated, and the resulting distribution of income available for interest, based on the 12 months ended June 30, 1935, was as follows:

		Item
D. & R. G. W. operation:		
Own lines (88 percent)	$2,641,638	A
Cut-off (12 percent)	360,025	B
	3,001,663	C
Motorway, dividends	11,600	D
D. & S. L. operation	912,960	E
	3,926,223	

The amounts of items B, D, and E, totaling $1,284,585, were applicable to the claim of the Finance Corporation, subject to a deduction of $457,747 in respect of the Salt Lake bonds which were to be redeemed under the plan then approved.

The debtor's segregation study, as was explained in our report, reflected the actual earnings of the system during the 12 months stated, adjusted for intercompany charges, maintenance costs, the revenues from certain traffic, the savings from consolidation, and other factors, all with the purpose of providing a basis for the new capitalization and distribution of securities. The record contains no analysis of system earnings of a later period, developed in the same way. The actual earnings of the Denver from 1935 to 1940, inclusive, adjusted for deferred maintenance in 1935–38 on the basis used in our previous report, show an average available income of $2,316,016 a year, corresponding to the amount stated above as item C. As to the portion of this total income that was derived from the operation over the cut-off, B, the record shows that the ratio, of the overhead freight tonnage moving via Denver to the Denver's total freight, increased from 6.5 percent in 1935 to 9.1 percent in 1939. Thus the 12-percent proportion, reflected in the original study, should not have diminished materially. It is accordingly adopted in the present computation. The average dividends from the Motorway companies during the 1935–40 period were $13,956 a year, instead of $11,600 as shown in item D. The actual earnings of the Salt Lake averaged $566,908 a year, item E. Revised on this basis the formula would be as follows:

	Distribution of earnings			Item
	R. F. C.	Amount	Ratio	
			Percent	
R. G. Western first-trust 4's		$866,190	35.4	
R. G. Western consolidated 4's		—67,257	—2.7	
Junction first 5's		126,362	6.2	
D. & R. G. consolidated 4's and 4½'s		754,095	30.8	
Equipment trusts		101,904	4.2	
Refunding and improvement 5's and 6's		256,800	10.5	
Subtotal		2,038,094		A
Denver cut-off operation	$277,922			B
Subtotal		(2,316,016)		C
Motorway dividends	13,956			D
Salt Lake operation	566,908			E
R. F. C. claim	858,786			
Interest on Salt Lake bonds	[1]449,360			
Net for R. F. C.		409,426	16.7	
Total		2,447,520	100.0	

[1] Consisting of 4 percent interest on the Salt Lake first-mortgage bonds, and 3 percent fixed interest and 1 percent prior contingent interest on the Salt Lake income bonds, as contemplated under the plan hereinafter approved.

The amounts of first-mortgage bonds, income bonds, and stock available under the plan herein approved, distributed on the basis of these percents to the several bond groups (including separately the Denver's bonds pledged with the Finance Corporation) and to the claim of the Finance Corporation, would produce the following primary allocations:

	First-mortgage bonds	Income bonds	Preferred stock, $100 par value	Common stock, $100 par value
R. G. W. first trusts	$12,832,512	$6,610,688		
R. G. W. consolidateds		1,167,192	$13,422,708	$4,863,300
Junction firsts	1,754,509	903,833		
D. & R. G. consolidateds	11,108,669	6,876,795	11,637,653	23,275,307
Refunding and improvements	3,075,200	1,922,000	4,036,200	10,186,600
Finance Corporation	7,197,881	4,587,727	1,591,601	
Total	35,968,762	22,068,235	30,688,162	38,325,207

The above allocations to the Finance Corporation comprise the new securities applicable to the pledged bonds of classes publicly held, and the new securities directly assignable to the claim by the 16.7 percent in the formula.

Neither of the foregoing analyses reflect anything for the Finance Corporation's second lien upon the securities pledged under the notes held by the Railroad Credit Corporation and the Chase National Bank. On the basis of present liquidation value, it appears that this equity may have some value, although the amount cannot be definitely determined. It is our opinion that it is less than $300,000.

As compared with these allotments to the Finance Corporation, the court allotted $4,312,853 of first-mortgage bonds and $8,540,931 of income bonds, stating that the first-mortgage bonds were intended to equal the amount of the loan for constructing the Dotsero cut-off, with interest to January 1, 1941, the effective date of the court plan. (The correct amount as of that date was $4,820,480, and as of January 1, 1942, was $4,802,040.) The committee, analyzing the court plan and taking into consideration the pledged collateral of classes that are publicly held, asserts that the court allowed only $1,163,293 of first-mortgage bonds to represent the other collateral, consisting principally of the Salt Lake and Salt Lake Western stocks. That this was not the theory followed by the court is shown by the following statements in its opinion of March 6, 1941:

The Reconstruction Finance Corporation receives $4,312,853 in first mortgage bonds, which equals the amount of their so-called cut-off notes secured by Denver & Salt Lake Western stock. This stock, it must be remembered, is really a first mortgage on the cut-off, there being no bonds or other indebtedness ahead of it. On its old advances the Reconstruction Finance Corporation received $8,540,921 in income bonds, and in return is asked to purchase $6,000,000 more of 4½ percent income bonds for cash, to be used to pay the trustees' obligations and reorganization expenses. * * * The new company acquires the Salt Lake Western (the cut-off) from the Reconstruction Finance Corporation by the payment of the original cost thereof in first mortgage bonds.

The matter of the treatment to be accorded the Finance Corporation claim also may be approached from the standpoint of the securities allocable to the collateral under pledge with the Finance Corporation. This consists of the bonds, stocks, et cetera, enumerated in our report in 233 I. C. C. 515, at page 524, except for the changes in the amounts of Salt Lake and motor companies' stocks, the amounts of these securities on pledge now being Salt Lake stock, 45,889 shares; Denver-Colorado Springs-Pueblo Motor Way, 73,710 shares; and Rio Grande Motor Way, 1,748[*] shares. Under the percentage treatment of claims reflected in the allocations shown just above, the 4 blocks of Denver bonds under pledge would be entitled to $1,318,626 of new first-mortgage bonds, $701,619 of new income bonds, $2,720,286 of preferred stock, and $4,064,282 of common stock. The $1,266,000 of Salt Lake income bonds would be entitled to substantially a like amount of new first-mortgage bonds, since the fixed interest rate and prior contingent interest rate are made the same for both issues under the present plan. To represent the approximate value of the Motorway stocks, Rio Grande Southern bonds, and Goshen Valley stock, $250,000 of new first-mortgage bonds should be assigned; for the 45,889 shares of Salt Lake stock, an equal number of shares of new common stock; and for the 36,310 shares of Salt Lake Western stock, $1,815,500 of new first-mortgage bonds, $907,750 of preferred stock, and $907,750 of common stock. The total amount of new first-mortgage bonds thus arrived at is $4,650,126.

At the hearings before the court, the committee introduced evidence consisting chiefly of a severance study which purported to show that, for the year 1939, on the most favorable basis of computation for the Salt Lake, the Denver's income available for interest would have been increased by $323,451 if the Salt Lake and Salt Lake Western had been operated as a single independent road, interchanging traffic with the Denver at Dotsero; that the Denver had so far lost money by the cut-off operation; that the $391,000

[*] This amount was later increased to 1,858 shares. See *Denver & R. G. W. R. Co. Reconstruction Loan*, 252 I. C. C. ——.

of income of the Salt Lake available for interest in 1939 would have been converted into a deficit of $182,229 by the severance; that if all the roads had been operated as a consolidated system in 1939 the income available for interest would have been $2,512,184, while with the cut-off lines divorced it would have been $2,064,368. The conclusion was that something like $500,000 a year was the maximum realizable value of the Salt Lake-Salt Lake Western to the Denver.

The study depends upon several basic and important determinations, including the division of rates between the two carriers if operating independently, the amount of traffic moving over the cut-off in 1939 which could have been diverted via Pueblo, the additional cost of handling such diverted traffic, and the feasibility of handling the Denver's interchange with the Rock Island at Colorado Springs. These are highly controversial questions. It is noted that the study shows an increasing money benefit to the system by the inclusion of the Salt Lake, as the total revenues rise above those of 1939. While the Denver's interchange at Pueblo and Denver are both increasing, the largest increase, in terms of revenue and by individual roads, between 1937 and 1940, was with the Burlington at Denver.

The severance study purports to measure the value of the cut-off to the Denver or the consolidated system by calculating the effect of its separate and competitive operation, using a given amount of overhead cut-off traffic, and assuming that, by solicitation on the part of the Denver, the Missouri Pacific, and the Rock Island, approximately 64 percent of such traffic could be diverted to the Denver's own line via Pueblo. The benefit of the debtor from the portion of the haul west of Dotsero on traffic brought to the debtor by the cut-off is not separately reflected in the study as a credit to the cut-off.

The situation here is distinctly different from that existing in the Chicago & North Western Railway Company reorganization referred to by the committee which caused the judge to state that, since the Milwaukee, Sparta and North Western Railway Company was a "bridge line," the only fair measure of its value to the system was a severance study. *In re Chicago & N. W. Ry. Co.* (1940), 35 Fed. Supp. 230, 240. That opinion clearly states that the Sparta line was built for the purpose of reducing operating costs by diverting traffic from existing routes to the new bridge route. In the case now before us, the cut-off route was constructed to attract a larger share of transcontinental traffic to the debtor's line, and is considered as indispensable to the future of the debtor. Neither the segregation nor the severance studies reflect these factors. Any

real value in the cut-off arising from such factors is based on the ability of the debtor to solicit traffic routed over the shorter cut-off route and the extent that such solicitation is successful. Obviously, such traffic could not be routed through Pueblo, a fact which places a limitation upon the applicability of a severance study to the situation. Continued increase in traffic which must be routed over the cut-off would unquestionably render the severance study presented by the committee entirely inapplicable to the debtor's situation. We are not convinced that the full traffic possibilities of the cut-off as yet have been developed.

The narrow conclusions drawn by the committee from the severance study would encourage the view that a separation of the cut-off and the debtor into separate systems would benefit the debtor. Yet if such separation occurred so that there was competitive solicitation between the two routes, certainly if the study correctly reflects the situation, the result would be disadvantageous to the debtor to the extent that it forced routing of traffic over the cut-off. None of the studies reflects the effect of such competition or of such solicitation.

Such an analysis of existing traffic and earnings does not, in our opinion, adequately represent what the situation of the system would have been at the present time, or would be in the future, if the short route via Denver had not been created. The committee's witness estimated the amount of new business that was attracted to the cut-off in 1939 at some 195,000 tons, or 12.6 percent of all the overhead business. The committee's exhibits, however, show that the Denver's proportion of the combined transcontinental freight tonnage of the Denver and the Union Pacific (composing the so-called central group) increased from 21.2 percent in 1935 to 25.4 percent in 1939, and the Denver's proportion of the combined transcontinental freight tonnage of six important trunk lines increased from 6.0 percent to 7.4 percent. In the same period, the Denver's total overhead traffic increased from 1,058,512 tons to 1,551,341 tons, the amount moving via Denver increasing from 466,719 tons to 785,042 tons. It seems obvious that this favorable showing was due in large part to the existence of the cut-off route, although there was evidence that to some extent the increase was due to the opening up of other railroad facilities.

Notwithstanding the severance study, the judge expressed the opinion that the cut-off is "absolutely essential if the debtor is to have a future." The committee itself shows that, with a traffic increase of 10 percent over 1939, the estimated value of the cut-off, on a severance basis, expressed in earnings available for interest on funded debt, would rise to $685,929. The showing clearly fails

in providing a reliable figure to substitute in the formula for the earnings of the cut-off, that is, the proportion of total earnings to be assigned to the claim of the Finance Corporation. We are of the opinion that the formula distribution, modified to reflect the results of operation in the period 1935 to 1940, and otherwise, as explained above, is supported by the present record, and, although the results of the severance study may not be disregarded in this connection, they should not be accorded controlling weight.

Considering the foregoing, it is our view that, on the basis of the court's allotment of first-mortgage bonds, $4,802,040 of such bonds should be allotted to the claim of the Finance Corporation. In order to adhere as closely as possible to the formula, insofar as the distribution of debt securities is concerned, the excess of $2,395,841 of first-mortgage bonds would be distributed among the other claims entitled to receive first-mortgage bonds, in proportion to the respective earnings; the amounts of new income bonds allocable to those claims under the formula would be correspondingly reduced; and the amount of income bonds allocable to the Finance Corporation claim would be correspondingly increased. In terms of total new debt—first-mortgage bonds and income bonds—there would be no change, and the allotment of stock would not be affected. The adjusted distribution then would become:

	First mortgage bonds	Income bonds	Preferred stock, $100 par value	Common stock, $100 par value
R. G. W. first trusts	$13,804,672	$5,638,528		
R. G. W. consolidated		1,167,192	$13,422,708	$4,863,300
Junction firsts	1,887,416	770,917		
D. & R. G. consolidated	12,166,638	5,818,827	11,637,653	23,275,307
Refunding and improvements	3,459,600	1,537,600	4,036,200	10,186,600
General-mortgage bonds				2,102,888
Finance Corporation	4,802,040	6,983,568	1,591,601	
Total	36,120,366	21,916,632	30,688,162	40,428,095

Appendix C shows the development of the percentage allotments to the claims of the several bond groups, based upon the above table.

From a consideration of the foregoing analysis of the segregation study, the severance study, and the other matters referred to, we conclude that the distribution of securities to the various creditor classes should be as shown in appendix A of this report, based upon consolidation of all the properties, or as shown in appendix B in the absence of consolidation.

The individual claims will now be discussed.

Finance Corporation claim.—We have explained the basis adopted for the treatment of the Finance Corporation's claim in connection with the general distribution of new securities. The above assignment of new bonds and preferred stock, based as it is in part on the application of the cut-off arbitrary, reflects any strategic value there may be in control of the Salt Lake and Salt Lake Western now held by the Finance Corporation. This question, and the considerations pointing to the desirability of a general consolidation of the properties, were discussed at some length in our report on further consideration, 239 I. C. C. 583. While we are still of the opinion that the cut-off traffic possibilities have not yet been fully realized, it is our view and we find that, under present and prospective traffic conditions and on the evidence presented, it is impossible to find any value in the cut-off control in addition to that reflected in the allocations made above. In this situation, and in view of the fact that the Finance Corporation is not required to take any new securities in providing the new money needed in the reorganization, the plan will not provide for an issue of management stock to the Finance Corporation as was done in the court plan.

The Finance Corporation urges us to recognize and allow for the rental payable under the Salt Lake Western lease and supplemental agreements, which the debtor's trustees have not yet elected to affirm or disaffirm. A petition for the payment of this rental was filed with the court on March 25, 1936, by the trustee of the Salt Lake Western, but has never been acted upon. The Finance Corporation has been advised that the total amount due under the lease, as of January 1, 1942, was $1,179,666. The Finance Corporation contends that, if the payment of such sum to it, as the holder of the Salt Lake Western stock, is impracticable, then a substantial additional amount of new first-mortgage bonds should be allotted. It also suggests recognition of the lease value by capitalizing a part of the future rental. The committee takes the position that these claims of the Finance Corporation with respect to recognition of the Salt Lake Western rental values are untenable.

Our conclusion in this matter is that in the absence of a decision by the court on the above-mentioned petition, or of some other appropriate action determining the amount of the Salt Lake Western trustee's claim for the debtor's use and operation of its property, it would be inappropriate for us to attempt to assign any given value to the claim for rental. However, we cannot ignore the possibility that this claim may be determined by the court to have a value. For that reason, we are of the view that we should dispose of the matter now by providing in the plan for such eventuality.

This we do by the provision that, in the event the rental or other use-and-occupation claim of the Salt Lake Western trustee against the debtor's trustees is allowed in whole or in part by the court, the money value of the award shall be deducted from the total claim, with corresponding adjustment on a ratable basis, of the allocations, both directly and to pledged securities of new securities herein allotted to the total claim. The adjustments thus made in the allotments of securities should not change the allotments of securities to creditors other than the Finance Corporation but should be effected by making appropriate change in the new securities issuable to the Finance Corporation under the plan. The foregoing provision for the claim for rental should be applied regardless of whether or not consolidation is effected under the plan.

The examiner's recommendation, in case there is to be no consolidation, was that new securities be allotted to the pledged securities of classes that are publicly held, on the basis of the new plan, and that, for the remainder of the claim, a 12-year collateral note for $7,500,000 be given the Finance Corporation, secured by the Salt Lake stock, Salt Lake Western stock, and the "outside" securities now under pledge. The Finance Corporation contends that, if consolidation with the Salt Lake fails, it is entitled to outright ownership of the collateral which it holds and that if it is deprived of such ownership an adequate recognition of its rights requires that the proposed 12-year secured note should be for a substantially larger amount than $7,500,000, should bear 4 percent fixed interest, and should be an actual obligation of the new company, rather than that the obligations of the new company should be limited to the proceeds of sale of the pledged securities and to the income from such securities, as suggested by the examiner.

We agree in principle with the Finance Corporation that it is entitled to the pledged securities in the event there is no consolidation. On a cash basis, however, it is not entitled to any amount in excess of its claim, and any equity in the pledged securities clearly would belong to the debtor's estate. We think, therefore, that to turn all the collateral over to the Finance Corporation outright would be unjustifiable. All the rights of the Finance Corporation will be recognized if all of the pledged collateral, including securities received for pledged securities of the principal debtor, be placed in escrow for the benefit of the Finance Corporation, and if it be permitted to negotiate a sale or sales of the collateral and to receive any funds yielded by the collateral through interest payments, dividends, or sales, until the claim shall have been liquidated, whereupon its right and interest in the remaining collateral would cease, and, on the other hand, if the claim shall not have been

fully satisfied within a specified period by such payments, the securities, or the portion thereof remaining undisposed of, would be reduced to possession by the Finance Corporation, subject only to the conditions that the new company be permitted at any time to acquire all of the securities remaining in escrow by payment of the balance due upon the claim of the Finance Corporation, and to purchase all of the stock of the Salt Lake and Salt Lake Western which the Finance Corporation shall have requested the escrow agent to sell, at the price or prices stated in the request. The purchase of such stock by anyone other than the new company should be subject to our approval.

Such an arrangement would, in effect, assign the pledged collateral to the Finance Corporation to the extent necessary for the full settlement of its claim, any securities remaining thereafter to revert to the new company. We think that a period of 6 years would allow all reasonable opportunity for a sale of the Salt Lake or Salt Lake Western stock, if such a sale be practicable, or any other suitable disposition of the deposited securities. During this period the Finance Corporation should be entitled to vote all the stocks held in escrow.

This provision for an alternate treatment of the Finance Corporation's claim, in the event there is no consolidation, is included in appendix B, showing the capital structure and distribution of securities approved on that basis.

Claims of the bondholders.—As has been stated, the distribution of new first-mortgage bonds and income bonds under the plan now approved is in accordance with the percentage distribution shown, based on the original earnings formula as adjusted. The allocation of new securities to the several classes of claims is set out in appendix A. The percents of claim shown represent adjustments to the nearest even figure from the percents developed by the formula, as set out in appendix C.

The Rio Grande Western first-trust mortgage is secured by a first lien on approximately 415 miles of line, of which 314 miles are main line between Crevasse and Ogden, Utah, and on equipment having a ledger value, less depreciation, of $17,637, as of December 31, 1936.

Preferred treatment of the bonds was given in the early plans developed under the earnings formula, because of the earnings available for interest, averaging about 1½ times requirements, and the high traffic density on this part of the system. The $15,190,000 of bonds outstanding in the hands of the public, bearing interest

at 4 percent per annum, matured on July 1, 1939. With interest accrued to January 1, 1942, the claim amounts to $19,443,200.

In the court plan, the claim (as of January 1, 1941) was to be settled on the basis of approximately 80 percent in new first-mortgage bonds and 20 percent in new income bonds. The committee accepts this treatment, as a concession to facilitate an early reorganization, but urges a modification of the terms of the new first-mortgage bonds to provide that the prior contingent interest thereon shall become fixed interest when the sum of fixed and prior contingent interest shall have been earned 1½ times in each of the 3 calendar years in any 5 successive calendar years, provided that such 3 years include the last 2 of such 5 years. The committee proposes that this provision apply to all new first-mortgage bonds issued in reorganization, as has been stated. We do not approve this provision. In our opinion, adequate treatment is afforded those receiving the new first-mortgage bonds through the provision that the contingent-interest payment of 1 percent is to be prior to other contingent interest and fully cumulative. The increase in fixed-interest requirements which would result from this provision is not justified by the record.

The Rio Grande Western first consolidated mortgage represents a second lien on the property subject to the first lien of the first trusts, and a first lien on approximately 283 miles of branch lines, the entire capital stock of the Utah Fuel Company, and equipment, having a ledger value, less depreciation, of $681,191, as of December 31, 1936. The $15,080,000 of bonds outstanding in the hands of the public, bearing interest at 4 percent per annum, will mature on April 1, 1949. With interest accrued to January 1, 1942, the claim amounts to $19,453,200.

Under the court plan, preferred stock was allocated to this claim. The parties contend that income bonds should be allotted for portions of the claim, ranging from 25 percent to 35 percent. Such contentions contemplate a much larger total amount of income bonds that we are now approving.

The distribution formula shows no earnings directly for the Rio Grande Western consolidateds, but they are entitled to any new bonds assignable to the first trusts in excess of the amount of that claim. On the basis of the total amount of new first-mortgage bonds and income bonds available under the capital structure herein approved, the spillover for the consolidateds consists of income bonds equaling approximately 6 percent of the total claim. Preferred stock is allocated to 69 percent of the claim, and common stock to the balance.

The debtor's formula gives effect to the lien on the stock of the

Utah Fuel Company, to the extent that the mortgage is credited with $83,333 for the annual earnings of the fuel company. This credit is of no practical effect, however, because of the large deficit in net railway operating income computed. The evidence as to the fuel-company property, which we have already mentioned, raises serious doubt that the foregoing figure represents the real earnings of the fuel company. In our opinion, these bondholders are entitled to receive the beneficial interest in the Utah Fuel Company stock, in addition to the reorganization securities allotted to them. The approved plan so provides.

The Junction first mortgage represents a first lien on the 62.08 miles of main line between Rifle and Grand Junction, Colo. There are $2,000,000 of bonds outstanding, matured on December 1, 1939, bearing interest at 5 percent. The total amount of the claim, with interest accrued to January 1, 1942, is $2,658,333.

In all the plans prepared, these bonds have received the same treatment as the Rio Grande Western first trusts, on the basis of full coverage of interest requirements and high traffic density. The earnings formula herein followed supports this treatment. Our allotment of new securities is the same as for the first trusts, i. e., on the basis of 71 percent in first-mortgage bonds and 29 percent in income bonds.

Among the debtor's objections to the court plan was the point that the Junction is not a debtor under section 77. All other parties have evidently assumed that the Junction could be merged or consolidated in the new system although it is not in trusteeship. It has no separate operating organization. The property was leased by the debtor on January 1, 1890, for a term of 50 years, and the leasehold interest is in trusteeship. The trustee has continued to operate the property since expiration of the lease, without renewal. Its stock is pledged under the Denver's refunding and improvement mortgage. The trustee of the Junction mortgage is also the trustee of the Rio Grande Western first-trust mortgage, and its counsel have always discussed the two claims on the same basis with respect to the plan and the rights of the two classes of bondholders. The court plan made no distinction because of the fact that the Junction is not in trusteeship. We shall not attempt to adjudicate the question but shall provide for the inclusion of the Junction in the plan, with provision for its consolidation into the reorganized company.

The D. & R. G. first consolidated mortgage represents a first lien on approximately 875 miles of standard-gage and 683 miles of narrow-gage line, including the debtor's main line from Denver to Rifle via Pueblo, and an 18-mile section between Grand Junction

and Crevasse. Also covered by the lien is equipment having a ledger value, less depreciation, of $4,708,523, according to the debtor's statement of the various mortgage liens, introduced at the 1937 hearings.

The bonds issued under this mortgage and outstanding in the hands of the public comprise $34,125,000 of 4-percent bonds and $6,382,000 of 4½-percent bonds, all of which matured on January 1, 1936. The total amounts of these claims, as of January 1, 1942, were $44,362,500 and $8,535,925, respectively. The distribution formula indicates that new first-mortgage bonds should be allotted to approximately 23 percent of the total claims, and new income bonds to approximately 10 percent. The remainder of the claim is allotted preferred stock and common stock, as shown in appendix A. In the court plan, the allotment of new first-mortgage bonds was for approximately 28 percent of the claim, and of income bonds approximately 16 percent.

The debtor's refunding and improvement mortgage represents a first lien on approximately 85 miles of standard-gage and 34 miles of narrow-gage branch lines, a junior lien on all other lines owned, and a first lien on equipment having a ledger value, less depreciation, of $7,268,622, according to the debtor's evidence at the 1937 hearings. A question arose as to part of the equipment, having a depreciated value of $1,333,252, and, as stated in our report, 233 I. C. C. 515, at page 570, a compromise agreement was reached by the interested parties whereby the equipment in question was deemed to be subject to the lien of the D. & R. G. consolidated mortgage. There are pledged under the refunding and improvement mortgage the shares of Junction stock, less directors' qualifying shares, the stocks of the three terminal companies hereinbefore mentioned, and $906,000 of the Junction's refunding bonds.

The issues of bonds under this mortgage include $2,000,000 of series A 6-percent bonds, due on October 1, 1974, and owned in equal parts by the Missouri Pacific and the Western Pacific Railroad Corporation, and $22,481,000 of series B 5-percent bonds, due on April 1, 1978. Of the series B bonds, $4,385,000 are pledged with the Finance Corporation and $6,096,000 are pledged with the Chase National Bank, leaving $12,000,000 outstanding in the hands of the public. The total amounts of the claims, as of January 1, 1942, were series A, $2,870,000, and series B, $16,350,000, a total of $19,220,000.

Under the distribution formula and the plan herein approved, each of these claims is recognized by the allotment of new first-mortgage bonds for 18 percent, new income bonds for 8 percent, and preferred and common stocks for the balance, as shown in

appendix A. In the court plan, the corresponding percents for the new bonds were 28 and 16.

For the properties under the first lien of the refunding and improvement mortgage, as of December 31, 1935, the report of the Bureau of Valuation showed $12,121,243, as the cost of reproduction new, less depreciation, plus lands and rights, which is far below the amount of the claims. As we stated in our report, 233 I. C. C. 515, at pages 570–571, the depreciated book value of the equipment subject to the direct first lien of this mortgage, as of December 31, 1936, was $6,005,357, and that of the equipment subject to the first lien of $1,805,000 of equipment-trust obligations was $6,575,955. If subsequent depreciation and retirements are considered, not to mention large acquisitions of more efficient equipment, the foregoing amounts would seem to represent maximum values for the equipment. In our adjustment of the debtor's earnings formula, the refunding and improvement mortgage received the benefit of an increase from 2 percent to 4 percent in the rate charged for use of equipment.

Our adjustment of the formula also eliminated the alleged loss in operating the branch lines subject to the lien of this mortgage. This further increased the earnings computed for the refunding and improvement bonds, but no attempt was made to allow for the system revenue which was contributed by the branch traffic, approximating $1,500,000 a year.

As we have indicated earlier, the formula reflects a distribution of the charges paid by the Denver in connection with the three terminal companies, so it would be improper to take these properties into account in alloting new securities to the claim of the refunding and improvement bonds.

The debtor's general mortgage represents a lien generally upon the property securing the refunding and improvement mortgage but junior thereto. Under the general mortgage, there were issued $29,808,000 of bonds, bearing 5 percent interest, and maturing in 1955. The total claim, as of January 1, 1942, is stated by the mortgage trustee at $42,057,755. The court plan assigned new no-par common stock to this claim on the basis of approximately 3⅓ shares for each $1,000 of claim. The mortgage trustee urges an allowance of 50 percent in new common stock, arguing that the improvements made on the railroad and its recent earnings justify a larger capitalization than that contemplated by the court.

We have given careful consideration to the court plan and the later evidence as to earnings, but, within the framework of the capital structure which we have now decided upon, the maximum allowance for this claim is that shown on appendix A, viz, one-half

share of common stock, having a par value of $100 a share, for each $1,000 of claim.

From the foregoing considerations, we find that the provisions herein made for the settlement of the claims described above will afford full recognition of the rights of the holders of such claims and will be fair and equitable to all parties.

The holders of bonds of the classes shown below should receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, substantially the following amounts of new securities: Rio Grande Western Railway Company first-trust bonds, $908.80 of new first-mortgage bonds and $371.20 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $77.40 of new income bonds, $890.10, par value, of new preferred stock, and $322.50 of new common stock; Junction first-mortgage bonds, $943.71 of new first-mortgage bonds and $385.46 of new income bonds; Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $299.00 of new first-mortgage bonds, $143.00 of new income bonds, $286.00, par value, of new preferred stock, and $572.00, par value, of new common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $307.63 of new first-mortgage bonds, $147.12 of new income bonds, $294.25, par value, of new preferred stock, and $588.50, par value, of new common stock; the debtor's refunding and improvement 5-percent bonds, $245.25 of new first-mortgage bonds, $109.00 of new income bonds, $286.13, par value, of new preferred stock, and $722.12, par value, of new common stock; the debtor's refunding and improvement 6-percent bonds, $258.30 of new first-mortgage bonds, $114.80 of new income bonds, $301.35, par value, of new preferred stock, and $760.55, par value, of new common stock; the debtor's general-mortgage bonds, $70.55, par value, of new common stock.

The provision for scrip will be as in our former plan.

Salt Lake bonds and stock.—Under the terms of the Salt Lake income mortgage, interest becomes fixed at 6 percent if consolidation with another road is effected. During the 10-year period 1931–40, the earnings of the Salt Lake available for interest averaged 4.34 percent per annum on the amount of income bonds outstanding and the average payment was 4.2 percent. From 1928 to 1931, and in 1935, 6 percent was paid. The available income during the 10-year period averaged $478,000. This sum approximates the annual income indicated by the severance study, hereinbefore mentioned, as representing the contributive value of the cut-off to the system. The court plan provides that the holders of the income bonds be

offered 4 percent fixed interest, and it is desirable that every reasonable inducement be made in order to effect the consolidation. But, as the committee's analysis of the situation with respect to relative earnings, et cetera, shows, the allowance of 4 percent fixed interest on the Salt Lake incomes is evidently unjustified when the new first-mortgage bonds offered to the debtor's bondholders and the Finance Corporation are to bear 3 percent fixed interest and 1 percent prior contingent interest, and moreover are not to be issued for the full amount of these claims. A further consideration is the fact that the percent of new first-mortgage bonds allocated to the Western present mortgages in the court plan is materially reduced in the plan herein approved.

As above stated, the court plan made the consolidation with the Salt Lake subject to the consent of the holders of at least 66⅔ percent of the income bonds outstanding. Including the bonds pledged with the Finance Corporation, the total principal amount outstanding is $11,000,000, and, if only 66⅔ percent assent to the plan, the nonassenting bonds would amount to $3,666,666.67. The refinancing of such an amount would, in our opinion, place an unduly heavy burden on the new company. We conclude that the required percent of assents should be 90, in order to avoid this difficulty. This figure is not an unusually high one in similar cases where a creditor group is asked to join voluntarily in a general plan of financial readjustment.

We find that the proposal to be submitted to the holders of the Salt Lake income bonds should provide for (1) an extension of the maturity of the bonds to the maturity date of the first-mortgage series A bonds to be issued by the new company, (2) the modification of interest terms to fixed interest of 3 percent per annum, and prior contingent cumulative interest of 1 percent per annum, payable when fixed and contingent interest, respectively, on the new first-mortgage bonds become payable, subject to the right to postpone any interest payments with the consent of the holders of three-fourths of the bonds outstanding, as in the case of the new first-mortgage bonds of the new company, and (3) the call for payment, or for refunding (at the convenience of the reorganized company), of income bonds not consenting. If the holders of not less than 90 percent of the total income bonds outstanding consent to the foregoing conditions within 90 days from the submission of the proposal to them, the properties of the Salt Lake will be merged or consolidated with those of the new system, including the Salt Lake Western, the Junction, and the Goshen Valley. The new company will then assume the fixed-interest obligation of the Salt Lake first-mortgage bonds. No additional issues of bonds

under the Salt Lake mortgages will be permitted. The liens of these mortgages will remain undisturbed, and the lien of the new company's mortgages will be junior thereto with respects to the Salt Lake properties.

The amount of Salt Lake stock outstanding in the hands of the public has been increased from 460 shares, shown in our previous reports, to 4,111 shares as a result of the release of 3,651 shares by the Finance Corporation. New income bonds were allotted to these minority holdings of stock in our former plan, the court plan, the proposed report plan, and the modification of the latter suggested by the committee. Such treatment is admittedly liberal in view of the treatment which we have given herein to the majority Salt Lake stock pledged with the Finance Corporation, and also in view of the reduced capital structure now contemplated. Moreover, an allotment of income bonds would tend to dilute the total issue. We accordingly find that substantial justice will be done by providing that the Salt Lake minority stockholders receive new preferred stock on the basis of 1 share for each share of Salt Lake stock. Since the Salt Lake is not in trusteeship, the action taken by the stockholders with respect to this offer will necessarily be voluntary, and if the holders of the Salt Lake income bonds reject the proposal to modify the terms of such bonds the offer to the stockholders will not be made and the stock will remain undisturbed.

Other claims.—The claim of the Chase National Bank on its note of $1,500,000 with interest at 6 percent from the date of the filing of the debtor's petition under section 77, in accordance with the contentions of the bank, amounts to $2,068,458. The proper interest rate to use in computing this claim has not been determined by the courts. Subject to such determination, as stated in our former plan, the note should be extended for a term of 10 years, bearing interest at 4 percent per annum, payable semiannually, but such interest should be contingent upon, and the payment thereof should be limited to, the total of interest and dividends paid by the new company on the collateral securing the new note or notes. The provisions of our former plan for the claim of the Chase National Bank should be modified only with respect to the new collateral to be pledged. The present collateral consists of $6,096,000 of the debtor's refunding and improvement mortgage 5-percent bonds. With accrued interest to January 1, 1942, the amount is $8,305,800. Under the plan herein approved, the new securities allocable to it consist of $1,495,044 of first-mortgage bonds, $664,464 of income bonds, $1,744,218 of preferred stock, and $4,402,074 of common stock. The plan provides for the pledge of these securities as collateral security for the new note.

The Railroad Credit Corporation, in its brief, explains that, as of June 30, 1941, the unpaid balance of the original loan of $500,000 had been reduced to $266,715.09 owing to the application of distributive shares credited against the debtor's account arising out of the fund administered by the Credit Corporation, and the amount of unpaid interest was $904.88, making a total claim of $267,619.97. Explanation is also made of an error in the statement by the court of the amount of the claim as of January 1, 1941.[6] The Credit Corporation advises that the amount of its claims, as of January 1, 1942, was $265,194. In its exceptions to the examiner's proposed report, the Credit Corporation states its position with respect to the court plan as follows: It objects to the court's proposal for the reason that the court proceeds on the theory that the Credit Corporation is indebted to the debtor, and, in providing for payment of its claim in cash, the judge deducted from the claim the debtor's undistributed book balance, which includes income earned upon the marshaling and distributing fund. Under the theory outlined in the court plan, distribution of more than 100 percent of the debtor's contribution to the fund would have to be made. The Credit Corporation states that is hardly to be expected. It contends that distributive shares do not constitute a debt to the debtor unless and until funds are available and a distribution is actually declared, set aside, or made.

The provisions for the Credit Corporation claim as stated in our modified plan will be retained, with appropriate revision of the amounts of new securities issuable against the $662,000 of D. & R. G. consolidated-mortgage 4-percent bonds, which, with interest accrued to January 1, 1942, amount to $860,600. The new securities allocable under the plan herein approved consist of $197,938 of first-mortgage bonds, $94,666 of income bonds, $189,332 of preferred stock, and $378,664 of common stock.

All equipment obligations of the debtor outstanding, any equipment-trust certificates which may be issued by the bankruptcy trustees or any other obligations under equipment leases or sales agreements, will be assumed or paid by the new company when they respectively become due. The interest of the holders of such obligations shall be deemed not to be adversely and materially affected by the plan, and submission to the holders shall not be necessary. The plan should not be construed as prohibiting the assumption of obligation and liability in respect of additional equipment obligations prior or subsequent to its consummation, if duly authorized under section 20a of the Interstate Commerce Act.

[6] The court plan provided for the payment of the balance of the claim in cash after deducting the amount due the debtor under the marshaling and distributing plan.

Future control.—The trustee of the Missouri Pacific contends that an equity exists for the debtor's present stock, that the Missouri Pacific should be permitted to acquire 50 percent of the new common stock on fair and reasonable terms, and that voting control should be lodged solely in the common stock, as it is at present. Counsel for the debtor contend that provision should be made for allotting management stock to the debtor with conditions attached defining the extent of any contribution that should be required from the debtor whether for management stock alone or for management stock and "securities secured on debtor's wants."

We have reaffirmed our previous finding that the equity of the debtor's stockholders is of no value. In our prior report, 233 I. C. C. 515, at page 581, we said:

> As we view the matter these are not questions for us to decide in promulgating a reorganization plan where we find that the present stockholders have no equity, and we do not consider it our duty in this case to decide for the new owners what affiliations with other systems will be most advantageous to the new company, or to fix a price for any stock which may be offered to the Missouri Pacific, Western Pacific, or other railroad companies. In order, however, to facilitate any reasonable plan which the new stockholders may adopt with respect to the acquisition of an interest by a larger system or systems, the following provision for the stock should be incorporated in the reorganization plan.

We have given consideration to all the representations which have been made in this connection, including the court's proposal to make the income bonds assigned to the Finance Corporation convertible into management stock, and have concluded that we should adhere to our position as previously stated, which, in effect, leaves the matter of control of the new company to future determination.

In the proceedings before the court, the Public Service Commission of the State of Utah renewed its previous objections to the merger or consolidation of the Salt Lake, as contemplated under the plan certified to the court. The same objection may be made to the plan herein approved. It is predicated on the belief that if the Salt Lake were kept separate the building of an extension from Craig, Colo., westward to Provo or Salt Lake City would be facilitated. This impelled the Utah interests to oppose the Denver's acquisition of control of the Salt Lake. As stated in our report, 233 I. C. C. 515, at page 550, our opinion is that a consolidation of the roads will not alter the present situation in such a way as to prejudice the construction of an extension westward through the Uintah Basin of Utah.

New-money requirements.—The amount of new money required in the reorganization will depend on the extent to which the trus-

tees may be able to pay off their outstanding certificates prior to consummation of the plan, the amount of cash available for the expenses of reorganization not already paid, and the provision to be made for the nonassenting income bonds of the Salt Lake.

Counsel for the committee, in their exceptions to the proposed report, assert that all the trustees' certificates may be paid before effectuation of the plan, and that, as a minimum, not less than $2,000,000 of certificates will have been paid without the need for new money. In support of this contention, counsel presented estimated income accounts, prepared by the respective managements of the Denver and the Salt Lake, for the year 1941, with the last 4 months estimated, indicating that the combined earnings available for interest would be $5,116,049, as compared with an estimate of $3,513,590 made at the hearing in May 1941. Also presented was a copy of a letter from the debtor's trustees stating their intention to begin paying off the certificates on February 1, 1942, and to continue to pay them off as soon as the resources will permit, subject to declines in traffic, increases in pay rolls, the approval of the court, et cetera.

By its report of August 26 1940, in this proceeding, 242 I. C. C. 629, division 4 fixed maximum limits of allowance for compensation and expenses of trust companies, committees, their counsel, et cetera, up to May 20, 1940, in the total amount of approximately $268,000. Previously, approximately $225,000 had been paid out of the debtor's estate, largely as compensation of the trustees, their counsel, and technical advisers. It is clear that our former estimate of $1,000,000 for total reorganization expenses does not apply to the present situation and that plan should be revised accordingly.

It is evidently impossible to estimate closely the amount of money which will be required to pay or refund the Salt Lake income bonds, the holders of which reject the proposal for modification of interest, et cetera, if the assents required for consolidation are obtained. The plan provides that the payment or refunding of the nonassenting bonds will be at the convenience of the new company. There will be no obligation upon the new company to redeem these bonds, although the incentive to do so would arise from the fact that 6 percent interest would be payable if the lines should be consolidated.

The actual earnings of the Denver available for interest in 1941 were reported at $4,503,690, and those of the Salt Lake at $515,746, a total of $5,019,436.

The Denver's actual cash position at the close of 1941 is shown by balance-sheet figures as follows: Cash on hand, $4,460,157; total current assets, $11,828,589; and total current liabilities, $10,-

292,313. For present purposes, there are deductible from total current liabilities the Chase Bank loan of $1,500,000, the Railroad Credit Corporation loan of $264,966, and $1,950,000 of the Finance Corporation loan. The result is net current assets of $5,251,242. The corresponding figure for the Salt Lake is $153,384.

The district judge stated in his recent opinion that the trustees considered that they should have a working balance of not less than $1,250,000. At the further hearing before us, the debtor's general auditor testified that $2,000,000 would be ample.

The Denver's cash position should permit the early application of about $3,750,000 to the payment of trustees' certificates, leaving $1,250,000 outstanding. To the latter amount may be tentatively added $1,000,000 to be used for the payment or refunding of non-assenting Salt Lake income bonds, in the event of consolidation, or for the payment of reorganization expenses, as circumstances may require. The plan accordingly provides (1) for a new loan in the amount of $2,250,000, subject to such increase or decrease as may be determined by the reorganization committee and approved by the court, but in no event to exceed $4,000,000, such loan to be obtained either from the Finance Corporation or through private channels, and secured by new first-mortgage bonds issued for that purpose in an amount equal to 125 percent of the amount of the loan, or by such other amount as shall be required by the lender and approved by us; and (2) as an alternative to such a loan, the plan provides that not exceeding $5,000,000 of new first-mortgage bonds may be issuable for sale to provide the new money required, as may be determined by the reorganization committee and approved by the court.

Voting trust for new stock.—The modified plan previously approved provided that all the preferred stock and common stock of the new company, except shares issued to qualify directors, should be deposited under an escrow agreement for a term of 10 years and that the voting trustees, subject to our approval, and with the consent of the holders of escrow receipts representing not less than a majority of the shares of preferred stock and common stock, respectively, might sell all or any part of such stock at such price or prices as might be deemed advantageous to the interest of the new company and its stockholders.

The court plan provided that the consent of two-thirds of the holders of class A common stock would be required for a sale. We approve this provision if restated so as to apply to the holders of escrow receipts representing not less than two-thirds of the stock. Giving effect to this change, the approved provisions for the voting trust will be as follows:

All the preferred stock and all the common stock issued by the new company in reorganization, excepting shares issued to qualify directors, shall be deposited under an escrow agreement with a bank or trust company designed by the court, and escrow receipts issued to persons entitled to receive such stock under the plan. The escrow agreement shall be for a term of 10 years from the date of creation of the trust, such term to be considered as beginning not later than 6 months after the confirmation of the plan, and shall provide that the reorganization committee, as voting trustees, may, subject to the approval of the Commission, and with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of preferred stock on deposit, sell all or any part of such preferred stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders; likewise the voting trustees may sell all or any part of the deposited common stock, with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of such common stock.

It shall be provided that all holders of escrow receipts shall be bound by the terms of any sale or sales which shall have been approved by this Commission and consented to as aforesaid, and the net proceeds of any sale or sales, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts for preferred stock and common stock, respectively, according to the class of stock sold. During the life of the escrow agreement, the holders of escrow receipts shall have the right to receive notice of all meetings of stockholders and to direct the voting trustees as to the manner in which the stock represented by the escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stock shall be voted in such manner as the voting trustees may determine. The reasonable compensation and expenses of the voting trustees, including counsel fees, shall be paid by the new company.

Reorganization committee.—Our former plan provided for a reorganization committee consisting of five members, two to be designated by the committee, one by the trustee under the debtor's refunding and improvement mortgage, one by the trustee under the general mortgage, and one by the Finance Corporation. The judge, pointing out that the properties of the debtor and secondary debtor are located almost wholly in the States of Colorado and Utah, urges that all the members of the reorganization committee be residents of these States, that all meetings of the committee be held in Denver, at the main office of the debtor, and that counsel

for the committee, if any are necessary, shall be appointed by the court. Later, the judge expressed the opinion that the property should be under the direct control of the court until the reorganization is completed; also that the insurance-group committee should be represented by only one member on the reorganization committee and that the court or some other proper authority should name one member to represent the public interests of the citizens of Colorado. In line with the latter suggestion we approve the designation of one member by the court, and in lieu of one member each as representatives of the debtor's refunding and improvement mortgage and the general mortgage, we are of the opinion that these groups may properly be represented by one member, to be designated jointly by the two mortgage trustees. The total number of members will remain at five.

Provisions for new bonds.—The court proposed that the interest on the new 4½-percent income bonds shall be payable only to the extent of three-fourths of the income available for the payment thereof, and that it be cumulative only to the extent that payable interest is unpaid. It would seem, as pointed out in the brief of the committee, that the purpose of this provision may have been to permit the company to apply more of its income to additions and betterments than would be the case under the interest provisions of our plan for the new income bonds. The proposal now appears unnecessary and is not approved.

In connection with the new first-mortgage bonds to be issued in the reorganization, our modified plan provided that additional bonds shall be issuable under certain conditions, and included the following (239 I. C. C. 583, 600):

> [3*] When on any interest payment date the aggregate principal amount of first-mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either 35 percent of total capitalization as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the mortgage trustee as a sinking fund a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, the payment to the capital fund, contingent interest, and sinking-fund payments for the retirement of income bonds as hereinafter prescribed.

Counsel for the insurance group suggest that the foregoing percentage figures of 35 percent and 60 percent be increased to 45 percent and 70 percent, respectively, so that "this sinking fund will constitute only a practical check on injudicious financing rather than a harsh and impracticable constraint on the new company."

The plan which included this provision did not provide that the

Salt Lake bonds be treated in the manner that is now contemplated, nor that interest charges would be divided into fixed, prior contingent, and contingent classes. Under the capital structure herein approved, the ratio of total fixed-interest debt[1] to total capitalization will, at the outset, exceed 35 percent. We approve the change to 45 percent, in the case of consolidation, and 40 percent if consolidation is not to be effected. The provision in question will be modified to read substantially as follows:

(2) If consolidation with the Salt Lake is effected in accordance with this plan, and when on any interest payment date for first-mortgage bonds the aggregate principal amount of new first-mortgage bonds outstanding, together with Salt Lake first-mortgage bonds and income bonds, plus all other funded debt bearing fixed interest, shall exceed either 45 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the trustee of the new first mortgage as a sinking fund, a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, prior contingent interest charges, the payment to the capital fund, contingent interest, and sinking-fund payments, as hereinafter prescribed; but, in the event such consolidation with the Denver and Salt Lake Railway Company is not effected, the foregoing requirement of 45 percent for total fixed interest bearing debt shall be 40 percent.

Counsel for the committee further request that the following provision of our modified plan* for the new first-mortgage bonds be omitted:

(4) No additional bonds of series A other than those to be issued under the plan may be issued, and no bonds may be issued of any series having a maturity on or before the maturity of the bonds of series A, except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition.

Counsel also request the omission of the corresponding provision (page 602) for the new income bonds reading:

(3) No income bonds other than those issued in connection with the plan shall be issued having a maturity on or before the maturity of the initial issue, except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition.

Our modified plan* also contained the following provision for the first-mortgage bonds, and a similar provision for the income bonds:

Additional bonds shall be issuable under the mortgage without limit as to amount, or within such limit as may be specified in the mortgage, having such dates, maturities, coupon rates, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission.

[1] Including as such all the new first-mortgage bonds bearing 3 percent interest and 1 percent prior contingent interest.

* Page numbers omitted.

In making this request, the committee contends that the limitation imposed in our plan as to the maturity of later issues of bonds would make it impossible for the new company to finance its needs, however, urgent, by means of bonds. We are persuaded that the plan should be modified by eliminating the restriction in question. *Chicago, R. I. & P. Ry. Co. Reorganization*, 247 I. C. C. 533, decided July 31, 1941. We approve the change in the present case, and our order will so provide.

The provisions for the new first-mortgage bonds will be modified by introducing a general sinking fund, the annual payments to equal one-half of 1 percent of the maximum principal amount of such bonds at any time authenticated and delivered, including bonds under pledge. The payments into this fund should be made from the available net income remaining after fixed interest and prior contingent interest, but before contingent interest on the income bonds.

The concluding paragraph in section E of our order of April 2, 1940, 239 I. C. C. 583, referred to future modifications or alterations of the new first mortgage, and read in part as follows*—

> provided that no such change or modification shall (*a*) alter or impair the obligation of the new company to pay the principal and interest of any bond at the time and place and at the rate and in the currency provided therein without the consent of the holder of such bonds * * *.

The following addition to the paragraph above referred to is approved and will be incorporated in the plan.

> Notwithstanding the limitation in clause (*a*) in this paragraph, the obligation of the new company to pay interest on bonds issued in the reorganization for presently outstanding securities (and any other bonds as to which it may be so provided in the mortgage or any supplemental indenture) may be modified by the concurrent action of the new company and of the holders of not less than three-fourths in aggregate principal amount of such bonds then outstanding, so as to postpone the time of payment of any particular installments of interest, or any described number of installments of interest, until any fixed or determinable date or until the happening of any specified contingency, not in any case later than the date when the principal of such bonds shall be or become payable; but no postponement shall be made of any installment of interest in excess of a cumulative total of 10 semiannual installments excluding installments paid or as to which due provision for payment has been made; and before any such postponement becomes effective the holders of such bonds shall become, and until all postponed installments of interest be paid or due provision for payment thereof be made shall remain, entitled to elect the smallest number of directors necessary to constitute a majority of the full board.

* Page number omitted.

In addition to the foregoing modifications of plan, certain minor revisions of our prior order are approved so that the plan will conform more nearly to plans recently approved by us, and these changes are incorporated in the present supplemental order.

We conclude that, upon the record previously made, the record in the court proceedings, and upon further hearing held by us, the report and order of April 2, 1940, approving a modified plan of reorganization for the Denver & Rio Grande Western Railroad Company, debtor, and the Denver & Salt Lake Western Railroad Company, secondary debtor, pursuant to section 77 of the Bankruptcy Act, as amended, should be further modified as herein specified, and that, as thus modified, the plan will meet the requirements of section 77 (b) and (e) of that act, will be compatible with the public interest, and should be approved.

An appropriate supplemental order will be entered.

MILLER, *Commissioner*, dissenting in part:

My separate expression in our prior report in this proceeding, 233 I. C. C. 515, 591, is equally applicable here. It is also my opinion that the common stock here should be no-par instead of $100 par value.

COMMISSIONER ROGERS did not participate in the disposition of this case.

* * * * * * *

(The appendices attached to this report are here omitted, being reproduced, slightly modified, as appendices to the Commission's last report which is hereinafter printed in full.)

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted May 18, 1943. Decided June 14, 1943

Upon petitions, the modified plan of reorganization of the Denver & Rio Grande Western Railroad Company, approved on July 13, 1942, pursuant to section 77 of Bankruptcy Act, as amended, further modified and approved.[1]

Appearances as in prior reports, and also *Malcolm Lindsey* and *L. H. Larwill.*

Third Supplemental Report of the Commission

BY THE COMMISSION:

Within the statutory period of 60 days from the date of our second supplemental report and order herein, July 13, 1942, 254 I. C. C. 5, approving a further modified plan of reorganization for The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor, pursuant to section 77 of the Bankruptcy Act, 11 U. S. C. 205, petitions requesting its modification were filed (1) jointly by counsel for the insurance-group committee, the United States Trust Company of New York, trustee of the Denver & Rio Grande consolidated mortgage, the Guaranty Trust Company of New York, trustee of the Rio Grande Western consolidated mortgage, the Chase National Bank of the City of New York, trustee of the debtor's refunding and improvement mortgage, and the Untermyer family group, this joint petition being accompanied by a request on behalf of the Central Hanover Bank & Trust Company, trustee of the Rio Grande Western first-trust mortgage and the Junction first mortgage, that the plan be modified as proposed; (2) by the Reconstruction Finance Corporation; (3) by the City Bank Farmers Trust Company, trustee of the debtor's general mortgage; (4) by the trustee of the Missouri Pacific Railroad

[1] Previous reports: 212 I. C. C. 105 and 709; 217 I. C. C. 107; 224 I. C. C. 574; 230 I. C. C. 515; 239 I. C. C. 583; 242 I. C. C. 629 and 721; and 254 I. C. C. 5.

Company; and (5) by the Chamber of Commerce of Alamosa, Florence, Leadville, Montrose, Salida, and Pueblo, Colo., jointly.

The abbreviated titles of railroad companies and others as used in our prior reports are followed herein.

Answers to the joint petition of the committee and others were filed by the Finance Corporation, the Moffat Tunnel Improvement District, and the City Bank Farmers Trust Company. A reply to the petition of the Finance Corporation was filed by the committee and others.

Pursuant to the provisions of subsection 77 (e) of the act, we have proceeded to a reconsideration of the proceedings under subsection 77 (d).[2]

By the terms of section 77 (d) of the act, we may, after rendering a report and order in which we have approved a plan of reorganization, upon petition for good cause shown, filed within 60 days of the date of our order, and upon further hearing if we shall deem necessary, in a supplemental report and order, modify any plan which we have approved, stating the reasons for such modification.

In the joint petition, the parties ask that, if further information as to the proposed modifications is desired, or if we have doubts as to the propriety of making any of them, an opportunity be given the petitioners to file briefs and present oral argument, and, if we deem it appropriate, to present further evidence. None of the other parties requested a further hearing.

We have denied the debtor's request for a further hearing, filed on May 1, 1943. We have also denied the petition of intervention filed by George A. Gaston, and thus his petition for a further hearing to consider the rights and status of the first-mortgage bonds of the Rio Grande Junction Railway Company.

The district court held a hearing on October 23–24, 1942, on a petition for the payment of interest on the debtor's bonds, and held another hearing on April 14–16, 1943, on petitions for the payment of rental by the debtor's trustees for use of the Salt Lake Western property, and for the payment in full of the claim of The Railroad Credit Corporation. At the close of the hearing, the judge announced that he would authorize the payment of rental for the Salt Lake Western, the amount to be fixed later, and also the affirmance of the lease of the Salt Lake Western and the trackage agreement with the Salt Lake. The judge entered an order on April 15, 1943, approving the payment of the Credit Corporation's claim in full,

[2] Subsection 77 (e) provides in part as follows: "If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection 77 (d) hereof."

and the release of $662,000 of Denver and Rio Grande consolidated-mortgage 4-percent bonds, held as collateral. These bonds, which had been subject to the second lien of the Finance Corporation under the terms of its loans to the debtor, have been, or will be, turned over to the Finance Corporation.

We have given consideration to these developments since the issue of our prior report and order, and have considered the testimony adduced at the court hearings where it appeared to concern the plan of reorganization, notably the analyses made of the debtor's operation of the cut-off and the Junction lines. Our comments as to such testimony appear later herein.

The proposals for modification of plan and our conclusions in connection with them are as follows:

Effective date of plan.—Our order provided that the effective date of the plan would be January 1, 1942, which date would determine the extent to which the claims of the creditors would be capitalized in new securities. The plan permitted the reorganization committee, subject to the approval of the court, to cause the issue of new securities to be dated as of a date other than January 1, 1942, but only if the creditors who receive such issue of new securities shall receive the same treatment in respect of accruals of interest as if such issue of new securities had been dated January 1, 1942.

In their joint petition the parties suggest that the foregoing provisions be eliminated and the following substituted:

> The reorganization committee shall determine and fix the effective date of the plan at any time on or between January 1, 1942, and the first day of the calendar month next preceding the date when the new securities are ready for delivery, provided, however, that the effective date shall not be later than January 1, 1944, unless the Commission hereafter on application of the reorganization committee enters an order approving some later date; the Commission reserves jurisdiction to approve any later date on application of the reorganization committee and such approval shall not constitute a modification of the plan.
>
> The new securities shall be dated and shall bear interest, or dividends, from the effective date of the plan.
>
> The amounts of claims referred to in the plan, and the amounts of new securities to be allotted to such claims under the plan, are to be computed as of the effective date. The amounts of new securities to be allotted are to be determined by applying in the amounts of the respective claims remaining as of the effective date, after any cash payments, the percentages set forth in the plan and in the appendix (the dollar amounts of such claims and the dollar amounts of new securities allotted as set forth in the plan and in the appendix are for illustration only.)

The petition states that it is conceivable that eventualties (particularly in regard to taxes) which cannot now be clearly foreseen

might constrain some postponement to a date nearer the time of the actual delivery of the new securities, and that the reorganization managers should be given discretionary powers to deal with that business problem. Reference is made to the provisions regarding the effective date of plan in *Florida East Coast Ry Co. Reorganization*, 252 I. C. C. 731, decided August 10, 1942.

In the *Florida East Coast case*, a flexible date for the new general-mortgage bonds was possible, because payments of interest not specifically provided for in the plan would not affect the distribution of securities under the plan. No such special circumstances exist in the present case, nor have any of the other parties suggested a change in the effective date. In addition, to many changes in the provisions for the determination and application of available net income, the joint proposal might, if adopted, involve either a major increase in the capitalization fixed or a scaling down of the allotment to the most junior creditor class in order to maintain the capitalization. The proposal is not approved. However, as more than a year has elapsed since the effective date fixed in the plan of July 13, 1942, and a later date would more nearly conform to the time of issue of the new securities, we conclude that the date should be changed to January 1, 1943, and that the plan should be based on the amount of the claims outstsanding as of that date.

In connection with the matter of the effective date of plan, the Finance Corporation asks that, in view of its claim for compensation in respect of the rental of the Salt Lake Western and because of the dividends being paid on the Motorway stocks, the plan should provide that nothing therein shall be construed as limiting or in any manner affecting the right of the Finance Corporation to apply, in its discretion, the income on and the proceeds of the collateral held by it to or toward the payment of the principal or interest, or both, to or upon its claim against the debtor prior to the consummation of the reorganization. We approve this proposal. The provision will be added as the second paragraph of section J of our order.

Except as indicated, no change will be made in sections A and K of the order, quoted above, and no modifications are necessary in section G, describing the determination and application of available net income.

New money requirements.—Our report of July 13, 1942, stated that the Denver's cash position should permit the early application of about $3,750,000 to the payment of trustees' certificates, leaving $1,250,000 outstanding. To the latter amount, $1,000,000 was tentatively added for the payment or refunding of nonassenting Salt

Lake income bonds, in the event of consolidation, or for the payment of reorganization expenses, as circumstances may require. The plan provided for a new loan in the amount of $2,250,000, subject to such increase or decrease as may be determined by the reorganization committee and approved by the court, but in no event to exceed $4,000,000, such loan to be obtained either from the Finance Corporation or through private channels. As an alternative to such a loan, the plan provided that not exceeding $5,000,000 of new first-mortgage bonds would be issuable for sale to provide the new money required.

This provision was made upon the basis of the Denver's cash position at the close of 1941, and the trend of earnings then indicated. The amount of cash on hand was $4,460,157, total current assets were $11,828,589, and total current liabilities $10,292,313. After deduction of the Chase Bank loan, the Railroad Credit Corporation loan, and a portion of the Finance Corporation loan from the total liabilities, the resulting net current assets of the debtor were $5,251,242. The corresponding figure for the Salt Lake was $153,384. The debtor's trustees considered that they should have a working balance of not less than $1,250,000, and the debtor's general auditor testified that $2,000,000 would be ample. The $5,000,000 of trustees' certificates were paid in 1942. On this basis, the parties to the joint petition proposed that the provision for new financing through a loan of $2,250,000 be eliminated and that the amount of new first-mortgage bonds issuable to the creditors be correspondingly increased.

Evidence introduced at the court hearings in October 1942, and April 1943, showed that, during 1942, $2,282,106 of equipment obligations under conditional-sales agreements were paid, about $624,000 was paid on certain new equipment, and the debtor's cash on hand at the close of the year amounted to $10,050,150. The debtor's income account for 1942 shows $17,429,772 available for fixed charges, after railway tax accruals of $4,985,816. For the first 2 months of 1943, the income available for fixed charges was $2,443,963.

The present cash position and earning power of the Denver are adequate assurance that any probable amount of cash required for paying the remaining reorganization expenses and the refunding or payment of nonassenting Salt Lake bonds can be met from funds on hand. We conclude that the former provision for a loan of $2,250,000 should be eliminated as an item of the new capital structure, but that the plan should still permit the new company to negotiate a loan, if necessary, as suggested in the joint petition.

Accordingly, section L of the order will be modified to read as follows:

Any cash that may, in the judgment of the reorganization committee, be needed in reorganization, but in no event to exceed $2,000,000, shall be advanced by the Reconstruction Finance Corporation or obtained through private channels and evidenced by a collateral note of the new company for a term of 12 years, secured by pledge of new first-mortage bonds in an amount equal to 125 percent of the loan, or such other amount of bonds as may be required by the lender and approved by this Commission. As an alternative to such a loan, not exceeding $2,250,000 of new first mortgage bonds may be issued for sale to provide the new money required, under terms and conditions to be determined by the reorganization committee and approved by the court and this Commission.

New capital structure.—Under the plan of July 13, 1942, the total capitalization of the new consolidated company was to be approximately $154,521,612, including a total debt of $82,994,255. Total fixed-interest charges were approximately $1,766,966, prior contingent-interest charges $473,494, contingent-interest charges $1,009,185, and total charges ahead of dividends on the preferred stock $4,235,039 per annum. We found that the value of the properties for the purpose of this proceeding was $154,521,612 and that the total capitalization upon consummation of the plan should not exceed approximately that amount. We found that the total fixed-interest charges should not exceed approximately the amount above stated, and we approved a provision of the plan whereby the payment of fixed interest on the new first-mortgage bonds might be deferred with the assent of the holders of a stated proportion of the bonds.

Under this former plan, the equipment obligations as of January 1, 1942, were shown in total amount of $9,139,605, including $2,667,605 of obligations under conditional-sales agreements. As has been stated, the latter obligations have been paid in full. The remaining equipment obligations, under the trusts of series D, E, F, G, and I, amounted to $5,758,000, as of January 1, 1943. The introduction of this figure in the capital set-up instead of the former amount of equipment obligations results in a reduction of $3,381,605, which has been effected through cash payments, reflecting the increased earnings.

Under the plan as now further modified, the capitalization of the new consolidated company, based on the claims outstanding as of January 1, 1943, would be $155,173,127, consisting of the equipment obligations and Salt Lake bonds; the Chase National Bank note; $38,573,680 of new first-mortgage bonds; $29,750,184 of new income bonds; $32,531,220, par value, of new preferred stock; and $35,167,585, par value, of new common stock. The determination

of the amounts of the new first-mortgage bonds, new income bonds, et cetera, and the basis of the new allocations are described later. The plan, on the basis of consolidation, is shown in detail in appendices A and C, attached hereto. Total fixed-interest charges would approximate $1,694,941, prior contingent-interest charges $498,318, and contingent-interest charges $1,364,133; and, including the payments to sinking funds and the capital fund, the total charges before dividends on the preferred stock would be $4,584,689. The fixed-interest charges stated are less than in the former plan. We find that there will be adequate coverage of such charges.

The estimated gross outlay under the debtor's new-equipment program, which is the result of the war situation, is $8,772,000. The debtor expected to make a cash payment of $2,793,960 in 1942 on account of 1,000 gondola cars, of which 780 cars had been delivered, but the payment was deferred. Beside the gondola cars mentioned, the acquisitions include 6 Diesel freight locomotives, 300 dump cars, and 200 freight cars, all to be delivered during 1943. It appears that the entire $8,772,000 would be payable in 1943, and the 5-year amortization plan, which was begun in 1942, would be carried out. Improvements to old equipment are estimated at $596,146 a year. The proposed amortization charges on both present and proposed equipment, plus the estimated depreciation charges on present equipment, the estimated expenditures for improvements to present equipment, and the estimated charges to depreciation of roadway and structures will aggregate approximately $4,751,111 in 1943, and about $5,305,111 in each of the 3 succeeding years. In addition, the projects for general additions and betterments, authorized but not completed in 1942, called for an expenditure of approximately $3,100,000. Ad valorem taxes for 1942 were estimated at $470,000, railroad unemployment taxes at $700,000, and Federal and State income taxes at $1,300,000. Later testimony indicates that the railroad unemployment taxes amounted to about $608,000 and the Federal income-tax liability to about $1,760,000.

On a cash basis, the program for purchases of new equipment, the payments in connection with present equipment, the estimated amount of taxes payable, and a reasonable allowance for general additions and betterments require a total outlay of approximately $16,600,000. Assuming the plan in effect as of January 1, 1943, the interest charges and payments to the capital fund and sinking funds would total $4,584,689. The sum of the two amounts is $21,184,689. If the combined income available for interest and taxes in 1942 is equaled in 1943, and if it be added to the total cash on hand as of December 31, 1942, the total will be approximately $36,-

858,000. On this basis, the total cash on hand at the close of 1943 will amount to about $15,600,000.

On an income-account basis, the cash payments for the new equipment would be charged to capital account and the charges to depreciation and amortization of equipment would be introduced as operating expenses. The proposed charge of $700,000 for depreciation of roadway and structures would also be made in 1943. Including the additional taxes, additions and betterments, interest payments under present equipment trusts, proposed improvements to present equipment, and the charges under the plan as stated above, the total deductions from available income in 1943 (if 1942 earnings were repeated) would be approximately $7,845,000, leaving a net available income of approximately $10,389,000 for 1943. As has been stated, the program required the payment of $8,772,000 in 1943 for the new locomotives and cars, and this would have to be paid out of cash resources.

It appears that on either the cash basis or the income-account basis the present earning power justifies the capital structure and annual charges under the plan herein approved, taking into consideration the new-equipment program, tax levies, et cetera, as they have been presented by the debtor's trustees. The traffic necessities of the war period probably account for as much as $10,000,000 of new investment, most of which is reflected in the amortization charges described.

We have reviewed in our previous reports the carriers' earnings record and have shown that in 1941, when the original improvement program was largely completed, the system income available for interest was $5,019,436. The committee's analysis of the earnings during the 5 years 1936–40, reflecting the unit costs of operation in 1940, indicated an average available income of $3,446,765 a year.

One of the debtor's trustees, at the court hearing in October 1942, referred to a report by the traffic department describing the new industries on the line and estimating that about two-thirds of them would continue in operation after the war. The gross revenues from traffic of $3,446,765, the total would be $6,446,765, and, if added to the earnings and $6,000,000 in 1944, with net revenues of possibly 50 percent of gross. If $3,000,000 be added to the above-mentioned average figure of $3,446,765, the total would be $6,446,765, and, if added to the earnings of 1941, the total would be $8,019,436. Under the new capital structure herein approved, the total charges before dividends on the common stock will be approximately $6,211,250, and the payment of a 5-percent dividend on the common stock would bring the total to $7,969,629. The

debtor's earnings in 1942 are recognized, but the uncertainties surrounding the economic situation negative any assurance of a long continuation of such earning power. Under the present program, the expenditures necessary to handle the abnormally heavy traffic incident to the war effort will be paid for out of the income produced by that traffic. It is not probable, in our opinion, that the debtor will have any large amount of excess revenue from this special traffic after these and other necessary charges are made. After consideration of the foregoing and all the information of record, we conclude that the value of the combined properties for the purposes of this proceeding is approximately $155,173,127 and that the capitalization of the reorganized system should not exceed approximately that amount.

As in the former plan, the effect of reorganization of the Denver without consolidation of the Salt Lake would be to eliminate from the new capital structure the $11,234,000 of Salt Lake bonds, the $411,000 of new preferred stock allocated to the Salt Lake stock outstanding in the hands of the public, and the new securities allocated directly to the claim of the Finance Corporation. The resulting new total capitalization of the Denver would be substantially $143,528,027, of which $76,240,322 would represent debt. Fixed-interest charges would total $1,742,945 per annum, including $556,-024 of interest on the Finance Corporation claim, which, however, as explained in the plan, is not to be an obligation of the new company but will be payable out of the proceeds of the securities to be placed in escrow for the benefit of the Finance Corporation. Total charges ahead of dividends would amount to $4,055,379. The plan on this basis is shown in appendixes B and C.

We find that there will be adequate coverage of fixed charges of the new company on the basis of reorganization without the Salt Lake, in the amount of $1,742,945, and that the value of the combined properties for the purposes of this proceeding, excluding the Salt Lake and Salt Lake Western, is approximately $143,528,-027.

New first-mortgage bonds.—The proposal to increase the allowable amount of new first-mortgage bonds by approximately the amount formerly fixed for new financing is approved. It will not increase the total capitalization or place any additional obligation on the new company.

The parties to the joint petition propose that the additional first-mortgage bonds be distributed 70 percent to the Rio Grande Western first trusts and the Junction bonds, the remainder going to the Denver & Rio Grande consolidated, the refunding and improve-

ment bonds, and the Finance Corporation, increasing the allotment to the Finance Corporation by approximately 1 percent of the former allotment. The reason given for the 70-percent treatment is that it would fill out the principal amount of the Rio Grande Western claim, as was done under the court plan, described in our prior report.

We are not persuaded that this method of distribution is fair to the creditors as a whole, and we are of the opinion that the modified amounts of first-mortgage bonds and other new securities should be allocated in the same manner as was followed in the plan of July 13, 1942. This will be more fully explained later. The modification of allocations sought by the Finance Corporation will also be discussed.

Section D of our order provided for a so-called excess-bond sinking fund, which, if consolidation is effected, would become operative when the amount of all funded debt bearing fixed interest exceeds either 45 percent of total capitalization or the result obtained by deducting the principal amount of funded debt bearing contingent interest, other than bonds issued under the first mortgage, from 60 percent of total capitalization.

In the joint petition, it is asked that the above figure of 60 percent be changed to 65 percent, and a similar change made in section G (6) of the order, so as to provide more initial leeway for additional first-mortgage bonds. The change is consistent with the plan suggested in the joint petition and also with the modified plan herein approved. It will be adopted accordingly.

In connection with the operation of the excess-bond sinking fund when consolidation is not effected, the joint petition requests no change in the provisions of our former order but points out that the plan should indicate that the $535,088 of annual interest shown on former appendix A as applicable to the Finance Corporation claim of $18,377,209 as of January 1, 1942, is not an obligation of the new company but is collectible only out of the securities to be deposited in escrow for the benefit of the Finance Corporation. Unless this be done, it is stated, the Finance Corporation claim might be deemed a fixed-interest debt and the excess-bond sinking fund on the first-mortgage bonds would immediately become operative. This is true both with respect to our plan of July 13, 1942, and the modified plan herein approved, and, although the provisions made under section K of our order as to the payment of interest on the claim are clear, we deem it advisable to add the suggested footnote on new appendix C referring to the interest item of $556,024, and reading as follows:

Payable only out of the proceeds of the escrowed securities and an obligation of the new company, as explained in the plan.

New income bonds.—Under the plan of July 13, 1942, on the basis of consolidation, the amount of new income bonds was $21,916,932, these bonds being allocated among the several claims as shown in former appendix A.

The proposal made in the joint petition is to fix the amount of income bonds at $29,816,062, an increase of $7,897,430. This would permit filling out the claims of the R. G. Western first trusts, the Junction bonds, and the Finance Corporation, and leave sufficient bonds with which to make increases in the allotments to the other groups. As justification for the proposal, the petitioners refer to the court plan, wherein $30,289,451 of new income bonds were shown, to the prospect of increased traffic from the plants recently located on the line, and to the desirability of giving the present creditors the benefit, in respect of railroad income taxes, of receiving bonds rather than stock for a portion of their claims.

Using round numbers, an increase of $8,000,000 in the total amount of new income bonds would increase contingent-interest charges by $360,000 a year, with a decrease of $400,000 a year in dividends, at 5 percent, on a like amount of preferred stock. It would increase the ratio of total debt to total capitalization from 53.7 percent to 58.9 percent. In the light of the debtor's earnings record, we find this change to be permissible. The modified plan herein approved shows an increase of $7,833,552 in the amount of income bonds, and the basis upon which the increased amount of bonds has been allocated is explained hereinafter. The allocations suggested in the joint petition are not approved.

New stock.—Since the amount and allocations of the new stock, both preferred and common, shown in the suggested plan accompanying the joint petition, are predicated on a distribution of senior securities which we do not approve, and as they are also based on the claims outstanding on January 1, 1942, it is unnecessary to discuss this treatment of the new stock. The attached appendixes show the amounts and allocations approved.

In connection with the allotments of new common stock under the plan of July 13, 1942, the trustee of the debtor's general mortgage objected to the assignment of $2,102,888 of stock to the claim represented by the general-mortgage bonds, this assignment being on the basis of 5 percent of the principal amount of the claim plus interest to January 1, 1942. The mortgage trustee, in its petition for modification of plan, directed attention to the improved earnings and operating efficiency of the road, urged the elimination of

the item of $2,250,000 for new money, and proposed that the common stock allocated to the general-mortgage bonds be increased by that amount. Later in its reply to the joint petition of the committee and others, the trustee contended that the total capitalization of the new company under the plan of July 13, 1942, was unduly conservative and should be modified by increasing the amount of common stock so that at least five shares could be allocated to each $1,000 of the claim of the general-mortgage bonds.

The first-mentioned request, if applied to a 5-percent allotment to the claim as of January 1, 1943, would mean adding $2,250,000 to $2,177,408, resulting in an allotment of $4,427,408, or 10.2 percent of the claim. Under the second request, it would be necessary to issue $17,346,669 more common stock in order to satisfy 50 percent of the claim, which would increase total capitalization by a like amount.

Substantial compliance with the trustee's first request is made possible as a result of eliminating the provision for immediate borrowing, which, by increasing the amount of new first-mortgage bonds, permits the issue of a corresponding additional amount of new common stock. The total capitalization is, therefore, not enlarged by assigning common stock to the general-mortgage bonds on the basis of 10 percent of the claim. The modified plan will so provide. The request for further increases in capitalization is inconsistent with our previous findings herein as to the value of the properties and is disapproved.

Allocation of new securities.—The new securities under the plan of July 13, 1942, were allocated to the various claims as of January 1, 1942, on the basis of the debtor's segregation formula, adjusted to reflect the system earnings during the period 1935–40, and further adjusted in respect of the claim of the Finance Corporation, as shown on former appendix C and fully explained in our report. The same formula has now been applied to the claims as of January 1, 1943, and to the amount of bonds and stock herein approved. The primary allocations have been modified by reducing the allotment of first-mortgage bonds to the Finance Corporation claim to $5,200,000. The facts and considerations upon which this determination is made are stated below under "Treatment of Finance Corporation claim." The detailed figures are shown in appendix D, which provides the basis for the other appendixes attached to this report, and supersedes former appendix C.

The holders of bonds of the classes shown below should receive for each $1,000 bond and all unpaid interest thereon as of the effective date of the plan, substantially the following amounts of

new securities: Rio Grande Western Railway Company first-trust bonds, $970.20 of new first-mortgage bonds and $349.80 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $266.00 of new income bonds, $970.90, par value, of new preferred stock, and $93.10, par value, of new common stock; Rio Grande Junction Railway Company first-mortgage bonds, $1,061.96 of new first-mortgage bonds and $317.21 of new income bonds; Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $318.92 of new first-mortgage bonds, $217.08 of new income bonds, $321.60, par value, of new preferred stock, and $482.40, par value, of new common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $329.03 of new first-mortgage bonds, $223.97 of new income bonds, $331.80, par value, of new preferred stock, and $497.70, par value, of new common stock; the debtor's refunding and improvement mortgage 5-percent bonds, $250.01 of new first-mortgage bonds, $159.61 of new income bonds, $310.75, par value, of new preferred stock, and $692.13, par value, of new common stock; the debtor's refunding and improvement mortgage 6-percent bonds, $264.61 of new first-mortgage bonds, $168.94 of new income bonds, $328.90, par value, of new preferred stock, and $732.55, par value, of new common stock; and the debtor's general-mortgage bonds, $146.10, par value, of new common stock.

In view of the recent decision of the United States Supreme Court in *Institutional Investors Group* v. *Chicago, M., St. P. & P. R. Co.*, 318 U. S. ——, we deem it desirable to set forth our conclusions as to the adequacy of the compensation flowing under the plan to the various classes of bondholders for the rights surrendered by them. These considerations are important, since the plan permits participation by interests wholly or partly junior to each of five of the debtor's mortgages, the liens of which have been described in our previous reports.

The Rio Grande Western first-trust 4's are not callable and are secured by a first lien on 412 miles of road, and 24 units of equipment,[3] the secured debt amounting to $48,680 per mile of road, without the equipment. The new first-mortgage bonds to be issued in exchange for 73.5 percent of the claim of the holders of these bonds are redeemable at an initial premium of not exceeding 5 percent, or such lesser amount as the reorganization managers may determine, and will constitute a first lien, in case of consolidation, on 1,731 miles of railroad, and the debt secured will be $22,284 per mile of first lien. They will constitute a junior lien on the 220

[3] These and similar figures stated later are based on the Bureau of Valuation report dated March 1, 1937, filed in this proceeding.

miles of the Denver & Salt Lake. The new income-mortgage bonds will be junior to the lien of the new first-lien bonds, and the debt secured, including all prior debt, will be $42,797 per mile of line on which the new first mortgage is a first lien.

While the old Western first-trust 4's required the payment of interest, together with interest on other securities, out of earnings between the levels of $445,932 and approximately $2,863,922, the securities to be issued in exchange for them, i. e., new first-mortgage and income-mortgage bonds, will require payments of interest out of earnings between the levels of approximately $139,089 and $4,506,979. The latter is the limit of earnings necessary for the interest payment on all the income bonds after a capital-fund charge of $750,000 and a sinking-fund charge of $200,489 for the benefit of the new first-mortgage bonds, imposed in the plan. The old securities, which matured in 1939, bore interest at the rate of 4 percent per annum. The average rate of the new securities to be received in exchange under the plan, i. e., first-mortgage and income-mortgage bonds, is 4.13 percent. Unpaid interest on the income bonds is cumulative to 18 percent. They have the benefit of a sinking fund provided for at the rate of one-fourth of 1 percent of the maximum amount of the bonds issued, or $76,808 for the amount of bonds provided for in the plan.

Since the old first-trust 4's have matured, their interest rate is not determinative of the income which the holders of these bonds should receive either in kind or in some equivalent form of compensation from the securities received in exchange.

The surrender of income position of the first-trust 4's results wholly from the allocation of income bonds for 26.5 percent of the claim. When it is considered that the sinking-fund and the capital-fund payments are responsible for $950,489 of the apparent loss of approximately $1,700,000 of income position, it appears that such loss is of small moment: The sinking fund is provided, and would be used, to retire the debt ahead of the incomes, and the capital fund is for a purpose for which expenditures would have to be made to keep the property in a position to perform its function, even under the old capital structure. Finally, since 73.5 percent of the new securities allotted to the first-trust 4's are first-mortgage bonds which draw upon earnings before the payments into the capital fund are required, i. e., between the levels of $139,089 and $1,694,041, and thus their earnings position, and, as shown above, their lien position, excels that of the old bonds, it is our view that the holders of the first-trust 4's are adequately compensated, through the allocation of securities provided for in the plan, for any rights surrendered as a result of such exchange.

The Rio Grande Junction bonds bore a coupon rate of 5 percent, but matured in 1939. They were not callable and are secured by a first lien on 62 miles of railroad, the debt secured amounting to $44,489 per mile. The loss-of-earnings position of these bonds and the off-setting features are almost identical with those of the first-trust 4's described above, although there is a slight difference in the percentage of new securities allocable. We conclude that the holders of these bonds are adequately compensated for the rights surrendered.

The petitions for intervention and further hearing filed by George A. Gaston, and referred to at the beginning of this report as having been denied, sought a determination of certain rights as to rental due for the Junction line and as to additions and betterments made thereon, in the light of the lease of 1889 and the supplemental agreements entered into by the Junction and the debtor as of December 1924. The petitioner's purpose was to request that, to the extent that we consider we are without jurisdiction to determine such rights, by reason of the fact that the Junction has not filed a petition under section 77, we should provide in the plan that the treatment accorded the Junction bondholders shall be without prejudice to their rights for rent during the period of the lease, and for an accounting of the earnings of the Junction.

The record contains much testimony and discussion relating to the Junction lease and the question of which system mortgage has a lien on the leasehold. We considered these matters in connection with our examination of the original segregation formula, and, regarding the modification of the lease, we expressed an opinion that there was no merit in the contention of the refunding and improvement mortgage trustee that the supplemental agreements, along with the transactions which followed their execution, were void. 233 I. C. C. 515, 570. Pending a final determination of the question by the court, we think that a further hearing and the presentation of additional evidence before us in behalf of the Junction bondholders would serve no useful purpose. Nor do we think it necessary to provide in the plan that the treatment accorded the Junction bonds is without prejudice to the rights of the bondholders for rent during the period of the lease. The claim, as established on the record before us, will be satisfied by the allotment of new securities shown in the plan.

As to the status of the Junction under section 77, we reviewed the facts in our second supplemental report, stating that we shall not attempt to adjudicate the question but shall provide for the inclusion of the Junction in the plan, with provision for its consolidation into the reorganized company. 254 I. C. C. 5, 27. The

accompanying order provides that four properties, including the Junction, shall be merged or consolidated to the extent legally possible, by transfer to the reorganized debtor or to a new company organized for the purpose.

The property of the Junction constitutes an unseparable part of the principal debtor's main line. Payments of interest on its bonds are in default. The debtor owns all of its stock, and the parties holding liens upon the stock and the lease are before us in this proceeding. The record is replete with evidence as to the earning power of the Junction. It is our view that public interest demands consolidation of the Junction with the reorganized company. In the light of the circumstances, we believe that the consolidation and the distribution of securities to the Junction bondholders should be upon a bankruptcy basis, under the provisions of section 77, and that the absence of the formality of the filing of the petition should not prevent such disposition of the matter.

In order to prevent failure of consummation of our entire plan, however, if there is delay in disposition of the Junction affairs, or to prevent holding up the plan pending extended reorganization proceedings for that company, the plan will provide that, in the event it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan with respect to the other debtor properties, the provisions for the Junction bondholders may be considered wholly separable, and the remainder of the plan consummated immediately. Under these circumstances, the Junction stock and lease would become assets of the reorganized company subject to the liens of its mortgages with provision for release in the event the consolidation is carried out, and the plan will provide for disaffirmance of the Junction lease in the discretion of the reorganization managers of the principal debtor and the judge.

The bonds issued under the Denver & Rio Grande consolidated mortgage, the so-called Eastern Consols, are not callable, and constitute a first lien on 1,553 miles of the main line of the debtor from Denver through Pueblo, Colo., to Rifle, Colo., and from Grand Junction, Colo., to Crevasse, Colo., the debt so secured amounting to $35,126 per mile. In addition, the mortgage is secured by a lien on 151 locomotives, 2,189 freight-train cars, 115 passenger-train cars and 482 units of work equipment. The rate-making value of all of this property indicated by the data of record is approximately $63,543,069, or nearly one-half the total for the system.

New first-mortgage bonds would, under the plan, be exchanged for 23.8 percent of the claim of the Eastern Consols, new income-

mortgage bonds for 16.2 percent, new preferred stock for 24 percent, and new common stock for 36.0 percent, of such claim. The new first and second mortgages would, in the case of consolidation, have liens as described above.

The Eastern Consols bore interest at the rates of 4 percent and 4½ percent, and matured in 1936. They did not have the benefit of any sinking fund. While they were entitled to payment of interest out of earnings between the approximate levels of $445,932 and $2,863,922, the securities allotted in exchange would be serviced from earnings at various levels in excess of $139,089 through the levels necessary to pay dividends on common stock. This apparent change in earnings position is offset by the new sinking fund and capital fund and by the increased rate of return obtainable from the new securities, i. e., slightly in excess of 4.5 percent for 64 percent of the claim and unlimited stock dividends for the remainder. Convertibility of the preferred stock into common stock serves also to compensate for change in earnings position and for surrender of lien and right to fixed interest with respect to 60 percent of the claim.

From a consideration of the foregoing and all other features of the plan, we conclude that the holders of the Eastern Consols are adequately compensated for the rights surrendered by them.

The Rio Grande Western consolidated-mortgage 4-percent bonds, sometimes referred to as the Western Consols, will mature on April 1, 1949, and are callable at par. The property subject to the first lien of this mortgage consists of 265 miles of main-line railroad west of Crevasse, Colo., 45 locomotives, 592 freight-train cars, 23 passenger-train cars, 167 units of work equipment, and the entire capital stock of the Utah Fuel Company, 100,000 shares. The evidence indicates a rate-making value of approximately $7,797,448 for this property, other than the fuel-company stock. The debt secured by the first lien amounts to $27,212 per mile of road, excluding the equipment. Under the plan, the old bondholders would receive directly the ownership, or the proceeds, of the fuel-company stock.

The Western consolidated mortgage constitutes a second lien on the property upon which the Rio Grande Western first-trust 4's are a first lien. The total debt secured by the combined first and second liens amounts to approximately $59,000 per mile, exclusive of equipment and collateral security.

The Western Consols now participate, through payment of interest, in earnings between the levels of $2,863,922 and $3,522,922. The securities allotted to them under the plan, i. e., 20 percent in new income bonds, 73 percent in new preferred stock, and 7 per-

cent in common stock, would receive interest and dividends out of earnings after the level of $3,142,846 is reached. Loss in earnings position and surrender of other rights, in our opinion, are offset by the possibility of increased return permitted by the 4½-percent income bonds, 5-percent convertible preferred stock, unlimited dividends on common stock, and the other features of the plan.

The debtor's 5-percent refunding and improvement mortgage bonds outstanding in the hands of the public, due April 1, 1978, are callable at 102½, and a sinking fund is provided for any bonds issued for the acquisition of equipment. No sums have been set aside in the fund for any of the 5-percent bonds now outstanding. The 6-percent bonds mature on October 1, 1974, and are callable at 107½. No sinking fund is provided for them.

The property subject to the first lien of the mortgage consists of 128 miles of branch lines, 150 locomotives, 9,816 freight-train cars, 113 passenger-train cars, and 119 units of work equipment, all having a total rate-making value of approximately $12,121,243.

The property subject to the second lien of the R. & I. mortgage consists of 1,818 miles of road having an indicated rate-making value of $71,340,517, and that subject to the third lien consists of 412 miles of road having an indicated rate-making value of $27,958,647. Various securities are pledged under the mortgage, the most important of which are the stocks of the Junction and the terminal companies. The average debt per mile secured by this mortgage and all prior liens amounts to $48,578 per mile of railroad, exclusive of equipment.

The holders of these bonds are allotted, under the plan, 17.7 percent of their claims in new first-mortgage bonds, 11.3 percent in new 4½-percent income bonds, 22 percent in the new 5-percent convertible preferred stock, and 49 percent in new common stock. The liens of the new securities are set out above. The total return to the holders of the R. & I's. from their new first-mortgage bonds, income bonds, and preferred stock, at the earnings level of approximately $6,200,000 a year, will equal 64 percent of present total requirements at an earnings level of approximately $4,462,000. In order to cover the full amount of present interest requirements, dividends of approximately $2.64 a share on the new common stock would have to be paid, which would require total earnings of $7,139,674.

The total annual interest requirements of the old refunding and improvement bonds was $720,000. The total annual interest and dividends on the bonds and preferred stock allotted to them under the plan is $461,910. They also will receive whatever dividends may be paid on 97,706 shares of common stock. Only about 32 per-

cent of the total interest and dividends payable on the new securities would come out of earnings before the level of $4,506,979 is reached, at which all the interest on the old bonds would be payable. Under the plan, there is a surrender-of-earnings position of these bonds with respect to 66 percent of their old requirements, or $477,430.

But the annual requirements of the new sinking funds provided for in the plan, which in part cause the change in the income position of the bonds, are $277,297, all of which goes to retire debt and improve the position of the junior securities allotted in exchange of the old bonds. In addition, the maximum annual requirements of the capital fund, which further dilutes the income position of the new junior securities so allotted, but which will be used to improve the debtor's property, amount to $750,000. It is our view that the various features of the new securities and of the plan as a whole adequately compensate the holders of the old refunding and improvement bonds for the rights surrendered by them under the exchange of securities provided for in the plan.

The allotments of securities to the holders of bonds of the five issues just discussed remain the same whether or not the consolidation plan becomes effective. We are of the view and find that the compensation to the holders of these five issues of bonds would be adequate under the provisions of the plan approved to take effect in case there is no consolidation.

On the basis of consolidation, the Finance Corporation should receive, in full settlement of its claim as of the effective date of the plan, $5,200,000 of new first-mortgage bonds and $8,700,605 of new income bonds.

The foregoing allotments to the bond groups will be unchanged in the event consolidation is not effected. The treatment of the claim of the Finance Corporation in such event will be by placing in escrow the pledged securities, or the reorganization securities issuable against certain items thereof, in the manner provided in the plan of July 13, 1942.

Appropriate changes will be made in section K of the order where the amounts of the new allocations are now modified, as indicated above. The provisions for extending the Chase National Bank note will be modified only to show the revised amounts of each class of new securities allocable to the bonds pledged as collateral security on the basis of the allocations herein approved for bonds of the same classes, respectively, and also on the basis of the interest accrued on the pledged bonds to January 1, 1943. In lieu of the securities formerly shown as replacing the collateral now held by the Chase National Bank, the new securities will consist of

$1,524,076 of first-mortgage bonds, $972,998 of income bonds, $1,894,332 of preferred stock, and $4,219,194 (42,192 shares) of common stock.

Voting trust; future control.—The plan of July 13, 1942, made the following provision with respect to the voting rights of the new stock:

> The preferred stock and common stock shall have equal voting rights, each share being entitled to one vote for the election of directors and in all matters of proprietary interest.

The plan provides, further, that all the preferred stock and common stock shall be placed in a voting trust under a 10-year escrow agreement, under which the stock of either class may be sold, subject to our approval, and with the consent of the holders of two-thirds of the escrow receipts representing the preferred and common, respectively.

The parties to the joint petition suggest the following modification of the first of these provisions:

> The preferred stock shall be entitled to one vote per share on the matters specified in section F hereinabove and on all matters as to which a vote by it is required by law but shall not be entitled to any other voting power except as follows: Until regular dividends at the maximum rate borne by the preferred stock shall have been paid in the amount of the equivalent of six quarterly dividends on all outstanding preferred stock, and thereafter so long as there shall be any unpaid accumulated dividends on the preferred stock equal, in the aggregate, to the equivalent of six quarterly dividends or more, the holders of the preferred stock, voting as a class, shall be entitled to elect two directors of the reorganized company, and the holders of common stock, voting as a class, shall be entitled to elect the remaining directors, which shall constitute a majority of the board. If, after the holders of the preferred stock shall have ceased to be entitled to elect directors (a) the reorganized company shall fail for 18 consecutive calendar months to pay full dividends on all preferred stock at the time outstanding or (b) accumulated unpaid dividends on the preferred stock of any series shall amount to the equivalent of six quarterly dividends or more, the holders of the preferred stock shall again be entitled to elect two directors until full current dividends shall have been paid on the preferred stock for the equivalent of six quarterly dividends and all dividends accumulated up to the end of the last preceding calendar year shall have been paid.
>
> The common stock shall be entitled to one vote per share.

The petitioners also suggest that the new preferred stock should be taken out of the proposed voting trust, with appropriate changes in sections I and M of our order.

In support of these proposals, the petitioners contend that the inclusion of the preferred stock in the escrow arrangement is unnecessary either to protect the continuity of management or to facilitate a sale of control to connecting lines. The number of shares of common stock outnumber the shares of preferred. It is

asserted that, if the common stock is voted as a unit, the preferred has no effective voting power except in such specific matters as to which the plan may confer the privilege of a separate class vote; that inclusion of the common stock, only, in the escrow arrangement would suffice both for continuity of management and for sale of control; inclusion of the preferred would actually obstruct the sale objective, if the plan means that the preferred, or some of it, must be sold if any stock is sold. If the preferred is issued for the purpose, among other purposes, of increasing as much as possible the market realization of the creditors receiving it, such creditors should not be compelled to leave such stock subject to the escrow provision, but should receive marketable certificates for the shares themselves. It is argued that, except for its special privilege of a class vote on specified corporate matters, the voting position of the preferred may be illusory and that it may be better protected by an assured power to obtain representation upon the board of directors upon default in its dividend payment than by a universal paper right of equal vote which might never procure any represenation; that the suggested change, so long as the representation is restricted to a minority of the board, might also improve the marketability of the common stock for sale to connecting roads. It is stated that the voting characteristics proposed are consistent with the listing policies of the New York Stock Exchange.

The restricted voting power suggested for the new preferred stock would be a distinct departure from the usual rule of equal voting rights per share for each class of stock issued. In several reorganization plans which we have approved, holders of the preferred stock are given the right to elect a majority of the boards of directors in the event preferred dividends at the maximum prescribed rate are not paid during 3 consecutive years. *Chicago, M., St. P. & P. R. Co. Reorganization*, 240 I. C. C. 257, *Chicago, R. I. & P. Ry. Co. Reorganization*, 247 I. C. C. 533, and *St. Louis S. W. Ry. Co. Reorganization*, 252 I. C. C. 325. A similar provision was proposed by the insurance-group committee itself under a suggested plan which accompanied the petition for modification of our plan of July 11, 1939, in this proceeding. At the same time, the committee was in favor of placing both the preferred stock and common stock in the voting trust, although the voting trustees were to be authorized to sell only the common.

The present joint proposal seems to be in line with that of the Missouri Pacific trustee, concurred in by the six chambers of commerce which filed a petition for modification of the plan, requesting an opportunity to acquire 50 percent of the voting control of the new company, where the control would be vested in the com-

mon stock. This matter was discussed in each of our previous reports, and it is still our view that the new owners of the property should decide what affiliations with other systems will be most advantageous. The plan for the voting trust was adopted in order to facilitate a possible sale of the new stock. It is also our view, as has been expressed in numerous cases, that the holders of preferred stock should have the same basic voting rights as the common, that is, one vote for each share in the election of directors and in all matters of proprietary interest. The question of marketability of the stock and the other considerations mentioned in the joint petition do not justify any departure from the rule. Accordingly, the proposal to limit the voting power of the preferred stock as described is disapproved, and no change will be made in the provisions for the voting trust.

In order to insure compliance with the listing requirements of the New York Stock Exchange under any future circumstances and also to permit cumulative voting, we deem it desirable to add a provision to the part of the order quoted above so that this part will read in full as follows:

> The preferred stock and common stock shall have equal voting rights, each share being entitled to one vote in the election of directors and in all matters of proprietary interest; provided, however, that the holders of the preferred stock, voting as a class, shall always have the right to elect not less than one-third, and in no event less than two, of the members of the board of directors. Cumulative voting shall be permitted.

Treatment of Finance Corporation claim.—The Finance Corporation considers the treatment of its claim under the plan of July 13, 1942, to be unfair and wholly inequitable and asks that the allocations be "substantially increased." Specific objections are made, in connection with the modified segregation formula, to the proportion of system earnings in 1935–40, which were allocated to the cut-off operation, to our alleged failure to allow for the profits of the lines west of Dotsero derived from traffic attracted by the cut-off, and to the alleged omission of the savings to be effected by consolidation. In connection with the final adjustment of the formula results (shown in tabular form in former appendix C) the Finance Corporation contended that consideration should have been given to the value of its second lien on the collateral pledged with the Chase National Bank and the Railroad Credit Corporation,[4] that the allotment of new first-mortgage bonds in the court plan was inadequate and should not have been followed, and that our analysis of the collateral pledged with the Finance Corporation

[4] As has been stated, the claim of the Railroad Credit Corporation has been paid.

on the basis of new securities assignable thereto was improper in at least two respects.

The debtor's segregation formula, based on operations during the so-called test period, namely, the 12 months ended June 30, 1935, showed the Denver's income available for interest to be $3,001,663, of which approximately 12 percent represented the earnings from the cut-off operation. Although, as we stated in our prior report, the record contains no analysis of the earnings of a later period, developed in the same way, we considered that the operating results during the period 1935–40 should be substituted for the test-period year in the formula calculations. As to the division of the earnings between the cut-off and the Denver's other operation in the 1935–40 period, we stated that the ratio of overhead freight tonnage moving via Denver to the Denver's total freight increased from 6.5 percent in 1935 to 9.1 percent in 1939, but we concluded that the original 12-percent division of the available income should be retained. At the court hearing in 1940, the Finance Corporation presented a study of the earnings from the cut-off operation in 1939, showing allocated gross revenues of $2,403,983 and earnings available for interest of $162,593. On this basis, the cut-off revenues were 11.1 percent of system revenues, but the available income was only 7.1 percent. At the court hearings in October 1942, and April 1943, witnesses testified that the proportion of system revenues contributed by the cut-off operation ranged from 25 percent in 1937 to 33.8 percent in 1942. It cannot be assumed from an increase in the ratio of tonnage that the income available for interest would change in the same proportion, as the Finance Corporation suggests. The tonnage figures may be regarded merely as an indication that the earnings of the cut-off operation in 1935–40 probably did not fall below 12 percent of the total, as established for the test period.

The Finance Corporation contends that the testimony indicates a profit of $1,300,000 in 1939, on the lines west of Dotsero, due to the cut-off traffic, and that neither the severance study nor the segregation study reflects this credit. In connection with the severance study, it was pointed out by the witness that the western lines would handle the bridge traffic whether it moved over the cut-off or via Pueblo. In any event, as was stated in our prior report, the severance study was not given controlling weight in the allocations arrived at by us. In order to provide for the contributed earnings in question in connection with the debtor's segregation formula, which we have used with various adjustments, it would be necessary to determine the earnings of the western lines in the period 1935–40, which were derived from the bridge traffic, and

to estimate what portion of such earnings had been attracted by the cut-off route and would not have moved over the Pueblo route. The record does not permit a satisfactory solution of this question, nor do we consider it essential to a fair determination of the treatment of the Finance Corporation claim.

The operating savings to be effected by consolidation of the Salt Lake are reflected in the debtor's segregation formula by the inclusion of an estimated amount therefor and are given weight in the primary distribution of new securities.

At the hearing before the court in April 1943, the Finance Corporation introduced an analysis purporting to show that the debtor's earnings from the cut-off operation available for interest in the year 1941 amounted to $1,149,700 and the earnings in the 4 preceding years ranged between $236,352 and $683,263. Studies introduced by the committee showed a deficit of $163,425 from operation of the cut-off in 1941, and larger deficits in the 3 preceding years. For 1942, the Finance Corporation showed a profit of $3,567,035, and the committee, a profit of $1,348,881. The differences arise primarily from different allowances of a mileage arbitrary to place the cut-off on a comparable basis with the longer route via Pueblo. Similar studies were presented for the debtor's operation over the Junction line.

The basic formula, modified and adopted by us for the plan, and explained in our prior reports, reflected an arbitrary of 175 miles for the cut-off. Insofar as the test year of the formula is concerned, the expert witnesses for the Finance Corporation and the committee agree on the use of this arbitrary and the cut-off earnings of approximately $370,000 which were computed on that basis. Their differences for the later years result principally from the fact that the committee's witness scaled down the arbitrary to 56 miles in 1939 and thereafter, for reasons explained. He regards the 175-mile figure as applicable only to the test year.

These studies were primarily concerned with the profit or loss from operating the Salt Lake Western line, since the amount of the rental was in question before the court. But the analyses covered the entire operation between Denver and Dotsero, and, as has been indicated, produced widely varying results. Whichever of these results might be accepted in lieu of the figure originally used, no new basis was supplied for a determination of the corresponding earnings of the other divisions of the system. All classes of creditors would be affected by such a change.

The final adjustments which we made in the allocations calculated by the modified segregation formula (former appendix C) resulted in the allotment of $4,802,040 of first-mortgage bonds,

$6,983,568 of income bonds, and $1,591,601 of preferred stock to the Finance Corporation. The considerations upon which these adjustments were made were stated at some length. We showed that the court, in its suggested plan, allotted $4,312,853 of first-mortgage bonds and $8,540,931 of income bonds to the claim, stating specifically that the allotment of the first-mortgage bonds was intended to equal the loan for constructing the cut-off. We found that the total amount of new first-mortgage bonds allocable to the pledged securities, on the basis of the plan then under consideration, was approximately $4,650,000. We discussed the committee's severance study and stated our conclusions. We were still of the opinion that the cut-off traffic possibilities had not yet been fully realized, but it was our view that on the evidence presented it was impossible to find any value in the cut-off control in addition to that reflected in the allocations made. It is our view that the additional evidence presented at the recent court hearing cannot be considered as in conflict with our conclusions as reflected in our adjustment of the allocations calculated by the formula, nor do we consider that such evidence justifies any change in the basis of our allocations of securities.

The analysis of pledged collateral, if revised to the extent necessary to conform to the plan herein approved, shows that there would be allocable to the bonds of classes publicly held $1,566,846 of new first-mortgage bonds, $1,388,150 of income bonds, $3,181,757 of preferred stock, and $3,861,910 of common stock. These allocations are on the same basis as if the pledged bonds were in the hands of the public.[5] With the assignment of new securities to the other collateral on the same basis as in our prior report, the total amount of new first-mortgage bonds assigned is $4,898,346. The value of the Finance Corporation's equity in the refunding and improvement mortgage bonds pledged with the Chase National Bank is, in our opinion, approximately $272,000. If this sum be added to the above-stated determination of first-mortgage bonds, the total would be $5,170,000.

For the Salt Lake Western stock pledged with the Finance Corporation, we allotted $1,815,500 of new first-mortgage bonds, $907,750 of preferred stock, and $907,750 of common stock, deeming such a set-up representative of a reasonable capital structure for a railroad such as the Salt Lake Western. The Finance Corpora-

[5] This was also the case in the previous analysis. Confusion was evidently caused by the phrase appearing in the second paragraph on sheet 14 of our prior report reading, "reflected in the allocations shown just above," which should have read, "reflected in the allocations shown in the table below." In the present allocations, account was taken of the transfer of $662,000 of D. & R. G. Consols to the Finance Corporation as a result of discharge of the Railroad Credit Corporation claim.

tion attempts to show that the Salt Lake Western is entitled to a larger proportion of first-mortgage bonds on the ground that the adjusted-earnings distribution used by us showed an income of $277,922 available for interest for the Denver's cut-off operation, and that the interest requirements of the Salt Lake bonds were more than covered by the separate earnings of the Salt Lake. The argument is not convincing, since the available income of $277,922 applies to the entire operation over the Salt Lake Western and Salt Lake, and, if capitalized by bonds, these bonds would theoretically be spread over both of these lines, notwithstanding the fact that bonds are already outstanding on the Salt Lake and are serviced by the earnings of the Salt Lake. We see no reason to alter our opinion as to the assignment of $1,815,500 of first-mortgage bonds to the Salt Lake Western stock.

The court's allotment of first-mortgage bonds to the claim of the Finance Corporation cannot be disregarded on the ground that the court failed to state what consideration it gave to the pledged collateral. The court was in possession of all the facts in this connection and had heard the testimony and arguments presented by the committee and the Finance Corporation, especially with regard to the value of the cut-off to the system. On the basis of the amount of the loan for constructing the Salt Lake Western, with interest to January 1, 1943, the new first-mortgage bonds assignable to the Finance Corporation claim under the court plan would be $4,983,590. If the estimated value of the Finance Corporation's equity in the Chase Bank collateral be added, the total would be approximately $5,255,000.

In our report of July 13, 1942, we found from a consideration of the entire record that the Finance Corporation was entitled to $4,802,040 of the first-mortgage bonds issuable under the plan therein approved, where consolidation is effected. Apportionment of the bonds now available for distribution between the classes of creditors on the ratios used in our prior report would give to the Finance Corporation $5,101,522 of the new first-mortgage bonds.

From a consideration of all of the foregoing, we conclude that $5,200,000 of first-mortgage bonds should be allotted, in the case of consolidation, to the Finance Corporation for its claim.

In section K of the plan, it is provided that, in the absence of consolidation, specific amounts of new securities shall be issued in respect of the pledged bonds of the publicly held classes, and that these new securities, together with the remaining collateral, shall be deposited in escrow, and escrow receipts issued to the Finance Corporation. Under the plan, all or any part of the escrowed securities may be sold at the request of the Finance Corporation, sub-

ject to specified conditions, and any or all receipts from the deposited securities, whether from sale, dividends, or interest, shall be paid over to the Finance Corporation and credited, first, against the interest accrued on the claim, any excess to apply on reduction of the principal. Conditions were prescribed as to the right of the new company to purchase the stock of the Salt Lake or of the Salt Lake Western, and as to the disposition of any securities or cash remaining after the Finance Corporation claim shall have been discharged, or after the expiration of the escrow agreement.

It was provided, further, that the amount of the Finance Corporation claim shall be adjusted and reduced in the amount of the money value of any award to the Finance Corporation which the court shall make upon the claim of the trustee of the Salt Lake Western against the trustees of the debtor in respect of the rental of the Salt Lake Western, and interest shall accrue only upon the total claim as so reduced. This latter provision, as stated in section J of our order, also applied in the case of consolidation, with appropriate adjustment in the allotment of new securities.

The Finance Corporation stresses the fact that we have not definitely found that its claim is fully secured nor found the cash value of the pledged securities. It argues that, if we deem the claim not to be fully secured and the value of the collateral less than the amount of the claim, it is entitled to receive all the pledged securities outright. In this connection, objection is raised to the proposal to reduce the allotment of securities by the amount of any award which the court may make for the rental of the Salt Lake Western line. The Finance Corporation insists that its right, as pledgee of the Salt Lake Western stock, to compensation for use of this line constitutes an expense of administration which must be provided for; that, unless the claim is fully secured, it does not follow that the new securities allocated should be reduced by reason of the rental payment, whether or not consolidation with the Salt Lake is effected; and, that the Finance Corporation cannot properly be deprived of its right to resort to every item of its collateral until full satisfaction of its claim is reached.

As we stated in our first report herein (July 11, 1939, 233 I. C. C. 515) the treatment accorded the Finance Corporation in both the debtor's plan and the committee's plan recognized the claim as fully secured. The plan which we then approved was predicated on this generally accepted position of the Finance Corporation and on certain considerations beyond the estimated value of the securities under pledge, including the fact that the Finance Corporation, as pledgee of the stocks of the Salt Lake and Salt Lake Western, held

a veto power in the consolidation of the properties, which formed the basis of the plan.

As a result of the record made at the court hearing on the plan and the opinions rendered by the judge, we modified our first plan so that consolidation was no longer made a prerequisite in the reorganization. Additional evidence has been introduced as to the earnings of the cut-off operation and the Salt Lake separate operation. The results of the application of the formula on the basis of the present record support the conclusion that the claim of the Finance Corporation is not fully secured. The allocation of securities to the Finance Corporation is on the basis of its collateral. We conclude that the plan should be modified to provide that, in case consolidation is accomplished under its provisions, no adjustment should be made on account of payments on the rent claim, in the securities allotted to the Finance Corporation claim.

In the event consolidation is not to be carried out; our plan provided, in effect, that the Finance Corporation should receive the full benefit of all the pledged securities, to the extent necessary to discharge the claim. Under this arrangement the pledged securities, or a part of them, may ultimately be reduced to possession by the Finance Corporation. Clearly the claim and the face amount of any note evidencing the indebtedness should be reduced by the amount of any rental allowance. The plan should be modified accordingly. Section J of the former order and so much of section K as relates to the Finance Corporation will be modified and consolidated as new section J, reading as follows:

* * * * * * *

(This statement of the provision is omitted here as it is shown in full in the plan.)

Matters connected with consolidation of the Denver & Salt Lake properties.—The plan of July 13, 1942, provides that the proposal for modification of the Salt Lake income bonds be submitted to the bondholders in the form determined by the reorganization committee, which shall report the results to the court, and, if the holders of 90 percent or more of the income bonds accept the proposal within 90 days of its submission, the consolidation of the Salt Lake properties with the debtor's properties shall be carried out as provided in the plan. Under this arrangement, the plan would be certified to the court and, if approved by it, would be submitted to the Denver's creditors for vote before the proposal to modify the terms of the Salt Lake is submitted to the holders of those bonds. The parties to the joint petition contend that the Denver's creditors cannot know what they are voting for unless the holders of the

Salt Lake income bonds shall have voted first, and suggest that the plan be first submitted to them by this Commission, and that the papers submitting the plan to creditors of the debtor shall state whether or not the holders of 90 percent in aggregate principal amount of the income bonds have consented to the plan.

The petitioners further contended that, if the plan is not accepted by the holders of 90 percent of the income bonds, then the Salt Lake Western lease and the Salt Lake trackage agreement should be disaffirmed and rejected by the plan, or at least that the plan shall not be submitted to the creditors for acceptance or rejection until such creditors and other parties shall have been given time to apply to the court for disaffirmance of the lease and trackage agreement and obtain an adjudication thereon.

The language used in the joint petition seems to indicate an intention to have the general plan, rather than the specific proposal for modification of bonds, submitted to the Salt Lake bondholders before submission to the Denver's creditors. It is immaterial, however, which document is meant. Not only is the Salt Lake not in process of reorganization under section 77, and its security holders not entitled to vote on the plan, but the act confers no power on anyone to put in force a part of a plan before the plan is confirmed. The submission of the plan to the classes of creditors entitled to vote for its acceptance or rejection is necessary before it can be confirmed. An informal vote secured from the holders of the income bonds would, of course, have no validity in the proceedings, nor would it be binding on the bondholders.

While those voting on the plan will not know in advance what the action of the holders of the Salt Lake income bonds will be, they will be able readily to ascertain from the plan the effect upon their interests in either event. The liens of the new bonds and the structure of the new system, with and without the Salt Lake, are clearly stated. Even if there were practicable means of submitting the proposal to the Salt Lake income bondholders we are not convinced that the alternative provided for in the plan is unjust to the debtor's creditors. The request for this modification of plan is denied.

Request was made in the joint petition that, if consolidation is not effected, the Salt Lake Western lease and the Salt Lake trackage agreement be disaffirmed, on the ground that the lease is impracticable and inequitable and if not disaffirmed would impose an unenforceable obligation on the new company. The petitioners objected to the possible assertion of a claim against the new company because of this "vague, unworkable, and excessive" lease. Replies to these contentions were filed by the Finance Corporation

and the Moffat tunnel interests, and all aspects of the matter were considered. In view of the ruling by the district court, that the lease and the agreement should be affirmed, any further discussion is unnecessary here, and no change will be made in section O of our order.

The joint petition proposes, as an incident to the other modifications of plan, that it be made clear that the Salt Lake Western is included within the plan, even in the absence of consolidation, and it is suggested that the following provision be included in section C of our order:

> Both the debtor and the secondary debtor shall be included within the plan and discharged from all their present debts (except those herein expressly provided to remain undisturbed) whether or not consolidation is effected.

This suggestion appears to arise from doubt as to the inclusion of the Salt Lake Western when its stock is preserved (under the plan for escrowing the Finance Corporation collateral, if consolidation is not effected) despite the extinguishment of the debt claim which is senior to the stock, that is, the note representing the loan to the Salt Lake Western. The Finance Corporation states that in the event, and only in the event, the plan makes fair and equitable provision for its claim, it will be willing to have the Salt Lake Western included in the plan and its indebtedness discharged as proposed.

We are of the opinion that the deposit of the Finance Corporation collateral in escrow for the benefit of the Finance Corporation, to the extent necessary to discharge the claim in full, as our plan provides, constitutes a fair and equitable provision for the claim and a discharge of the debt to the Finance Corporation in the event of no consolidation. As stated in the plan, no actual consolidation of the Salt Lake and Salt Lake Western will take place if the required consent of the Salt Lake income bondholders is not obtained. We approve the insertion of a statement that the plan is applicable to the Salt Lake Western as well as the Denver. We do not deem it necessary to provide for the discharge from debts as that situation will result from the provisions of the statute.

Assumption of obligations under the Salt Lake mortgages.—The plan of July 13, 1942, provided that the new company, in the event of consolidation of the Salt Lake, should assume the obligation to pay fixed interest at 4 percent on the Salt Lake first-mortgage bonds outstanding and the annual interest, as modified, on the Salt Lake income bonds. The terms of the Salt Lake first mortgage provide that, in the event of consolidation, the corporation into which the company is merged shall expressly assume the due and punc-

tual payment of principal and interest of all bonds. The income mortgage provides that the new corporation shall pay in cash all unpaid cumulative interest on the bonds and shall expressly assume the payment of principal and interest.

In view of this situation and on our own motion, we shall modify the provision under section K of our order (the third paragraph from the end of that section) to read as follows:

> In the event of consolidation with the Salt Lake on the basis herein provided, the new company shall assume all the obligations under the two Salt Lake mortgages, as stated therein in case of a merger into any other company, including the assumption of the obligation with respect to the payment of the principal and interest of all bonds now outstanding, except as the terms of the Salt Lake income bonds shall be modified, as provided above. No additional bonds shall be issued under either of the Salt Lake mortgages. The new company shall also assume the present tunnel contract, and the trackage agreement shall be canceled.

We conclude:

1. That, upon the petitions filed, the report and order of this Commission dated July 13, 1942, approving a modified plan of reorganization for the debtor and the secondary debtor pursuant to section 77 of the Bankruptcy Act, as amended, should be further modified as herein specified, and that as thus further modified, the plan will meet the requirements of section 77 (b) and (e) of the act, will be compatible with the public interest, and should be approved.

2. That, except as the plan shall be so further modified, the petitions for its modification should be denied.

3. That, except as modified herein, the findings and conclusions stated in our report of July 13, 1942, should be reaffirmed.

An appropriate supplemental order will be entered.

MILLER, *Commissioner*, dissenting in part:

Although the total capitalization approved in this report is nearer to what I think is justified than that approved in our original report, 233 I. C. C. 515, due to changed conditions affecting this carrier since that decision, it is still in the neighborhood of 10 percent too high. Otherwise, my separate expression in the second supplemental report, 254 I. C. C. 5, is applicable here.

APPENDIX A

Approved modified plan on the basis of consolidation with the Denver & Salt Lake

	Claims as of Jan. 1, 1943	Undisturbed or extended	First-mortgage bonds, 3 percent fixed interest, 1 percent prior contingent interest		Income bonds, 4½ percent contingent interest		Preferred stock, 5 percent		Common stock, $100 par value	
			Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount
			Percent		*Percent*		*Percent*		*Percent*	
Equipment obligations	$5,736,000	$5,736,000								
Rio Grande Western first-trust 4's	20,000,800		73.5	$14,737,338	26.5	$5,313,462				
Rio Grande Western consolidated 4's	20,036,400				20	4,011,280	73	$14,641,172	7	$1,403,948
Rio Grande Junction first 5's	2,736,333		77	2,123,916	23	634,417				
Denver & Rio Grande consolidated 4's	53,727,500		23.8	10,883,945	16.2	7,407,855	24	10,974,600	36	16,461,000
Denver & Rio Grande consolidated 4½'s	8,823,115		23.8	2,099,903	16.2	1,429,343	24	2,117,548	36	3,176,321
Refunding and improvement 5's	16,950,000		17.7	3,000,150	11.3	1,915,150	22	3,729,000	49	8,305,500
Refunding and improvement 6's	2,990,000		17.7	529,230	11.3	337,870	22	657,800	49	1,465,100
General-mortgage 5's	43,549,155								10	4,354,816
Chase National Bank note [1]	2,156,456	2,156,456								
R. R. Credit Corporation note, paid May 17, 1943										
R. V. C. notes	13,900,695			5,300,000		8,700,695				
Unsecured claims, approximate	440,000	no equity								
Total, Denver & Rio Grande Western	183,161,366	7,978,456		38,573,680		29,759,184		32,120,120		35,167,585
Denver & Salt Lake Securities: [2]										
Stock held by public 4,111 shares [3]								411,100		
								32,531,220		

[1] New securities to be issued for pledge as collateral on Chase National Bank note extended. First-mortgage bonds, $1,534,076; income bonds, $972,998; preferred stock, $1,894,332, and common stock, $4,219,194.

[2] First mortgage 4's, $1,500,000, assumed as to principal and interest, and income 6's, $9,734,000, also assumed as to principal and interest.

[3] Assigned 4,111 shares of new preferred stock.

APPENDIX B

Approved modified plan without consolidation with the Denver & Salt Lake

	Claims as of Jan. 1, 1943	Undisturbed or extended	First-mortgage bonds, 3 percent fixed interest, 1 percent prior contingent interest		Income bonds, 4½ percent contingent interest		Preferred stock, 5 percent		Common stock, $100 par value	
			Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount
			Percent		*Percent*		*Percent*		*Percent*	
Equipment obligations	$5,758,000	$5,758,000								
Rio Grande Western first-trust 4's	20,050,800		73.5	$14,737,338	26.5	$5,313,462				
Rio Grand Western consolidated 4's	20,056,400				20.0	4,011,280	73	$14,641,172	7	$1,403,948
Rio Grande Junction first 5's	2,758,333		77.0	2,123,916	23.0	634,417				
Denver & Rio Grande consolidated 4's	45,727,500		23.8	10,883,145	16.2	7,407,855	24	10,974,600	36	16,461,900
Denver & Rio Grande consolidated 4½'s	8,823,115		23.8	2,099,901	16.2	1,429,345	24	2,117,548	36	3,176,321
Refunding and improvement 5's	16,950,000		17.7	3,000,150	11.3	1,915,350	22	3,729,000	49	8,305,500
Refunding and improvement 6's	2,990,000		17.7	529,230	11.3	337,870	22	657,800	49	1,465,100
General-mortgage 5's	43,548,155								10	4,354,816
Chase National Bank note [1]	2,158,458	2,158,458								
R. R. Credit Corporation notes, paid May 17, 1943										
R. F. C. notes [1]	13,900,605	[2] 13,900,605								
Unsecured claims, approximate	440,000	no equity								
Total, Denver & Rio Grande Western	183,161,366	21,817,063		33,373,680		21,049,579		32,120,120		35,167,585
Denver & Salt Lake securities:										
Stock held by public, 4,111 shares, undisturbed										
First mortgage 4's		1,500,000 (undisturbed)								
Income 6's, including $1,266,000 held by R. F. C.		11,000,000 (undisturbed)								

[1] New securities to be issued for pledge as collateral, Chase National Bank note, extended: First-mortgage bonds, $1,524,076; income bonds, $972,998; preferred stock, $1,894,332; and common stock, $4,219,194.

[2] Note: R. F. C. claim to be provided for by depositing the pledged securities in escrow for a specified period, the receipts from sales, dividends and interest to be applied first to the payment of interest on the claim of $13,900,605 at 4 percent per annum, any excess to be applied to reduction of principal. For complete details see plan.

New securities to be nominally issued to R. F. C. in respect of its collateral of classes publicly held

	First-mortgage bonds	Income bonds	Preferred stock	Common stock
D. & R. G. consolidated 4's	$460,839	$313,681	$464,712	$697,068
R. G. W. first trust 4's	9,702	3,498		
R. G. W. consolidated 4's		371,070	1,354,406	129,874
Refunding and improvement 5's	1,096,305	699,901	1,362,639	3,034,968
Total	1,566,846	1,388,150	3,181,757	3,861,910

APPENDIX C

Capitalization and annual charges (see note below)

	On basis of consolidation with Denver & Salt Lake		Denver & Rio Grande Western without Denver & Salt Lake	
	Principal	Annual charges	Principal	Annual charges
Equipment-trust obligations	$5,758,000	$139,989	$5,758,000	$139,989
Chase National Bank note	2,158,458	[1] 45,722	2,158,458	[1] 45,722
R. F. C. claim (see plan)			13,900,605	[2] 556,024
Denver & Salt Lake first-mortgage bonds, 4 percent interest	1,500,000	60,000		
Denver & Salt Lake income bonds, 3-1 percent interest	9,734,000	292,020		
	19,150,458	537,731	21,817,063	741,735
New first-mortgage bonds, 3-1 percent interest	38,573,680	1,157,210	33,373,680	1,001,210
Total fixed interest	57,724,138	1,694,941	55,190,743	1,742,945
Capital fund, maximum payment		750,000		750,000
Prior contingent interest, 1 percent		[3] 498,318		[4] 348,978
Sinking fund for first-mortgage bonds, one half of 1 percent		[5] 200,189		[5] 182,323
		3,143,748		3,034,246
New income bonds, 4½ percent	29,750,184	[6] 1,364,133	21,049,579	[7] 972,606
Sinking fund for income bonds, one-fourth of 1 percent		[5] 76,808		[5] 58,527
Total debt, interest, payments to funds	87,474,322	4,584,689	76,240,322	4,055,379
New 5-percent preferred stock, par value $100	32,531,220	1,626,561	32,120,120	1,606,006
New common stock, par value $100	35,167,585		35,167,585	
Total capitalization	155,173,127		143,528,027	

[1] Fixed interest on the $1,524,076 of new first-mortgage bonds assigned as part of the collateral for new note to Chase National Bank.

[2] Payable only out of the proceeds of the escrowed securities, and not an obligation of the new company, as explained in the plan.

[3] Comprising prior contingent interest on:

New First-mortgage bonds $38,573,680	$385,737
New first-mortgage bonds assigned as part of collateral for new note to Chase National Bank, $1,524,076	15,241
Denver & Salt Lake income bonds	97,340
Total	498,318

[4] Comprising prior contingent interest on:

New first-mortgage bonds, $33,373,680	$333,737
New first-mortgage bonds assigned as part of collateral for new note to Chase National Bank	15,241
Total	348,978

[5] Including bonds to be nominally issued for pledge.

[6] Comprising contingent interest on:

New income bonds, $29,750,184	$1,338,758
New income bonds assigned as part of collateral for new note to Chase National Bank (only so much as necessary to fill out 4-percent interest on the note)	25,375
Total	1,364,133

[7] Comprising contingent interest on:

New income bonds, $21,049,579	$947,231
Part of interest on new income bonds assigned to Chase National Bank note, as in footnote 6	25,375
Total	972,606

NOTE.—The above statement does not purport to include the obligation or charges incurred through the new equipment program begun late in 1942 to facilitate the handling of traffic connected with military establishments and plants. See the accompanying report for details as to this program, new tax requirements, et cetera.

Distribution of new securities per $1,000 of present bonds with accrued interest

	First-mortgage bonds	Income bonds	Preferred stock	Common stock
Rio Grande Western first trusts ($15,190,000)	$970.20	$349.80		
Rio Grande Western consolidated's ($15,680,000)		266.00	$970.90	$93.10
Junction firsts ($2,000,000)	1,061.96	317.21		
Denver & Rio Grande consolidated 4's ($34,125,000)	318.92	217.08	321.60	482.40
Denver & Rio Grande consolidated 4½'s ($6,382,000)	329.03	223.97	331.80	497.70
Refunding and improvement 5's ($12,000,000)	250.01	159.81	310.75	692.13
Refunding and improvement 6's ($2,000,000)	294.61	168.94	328.90	732.55
General 5's ($29,808,000)				146.10

APPENDIX D

Development of new allocations on basis of consolidated system

	Claims as of Jan. 1, 1943	New first-mortgage bonds					New income bonds				Preferred stock	Common stock
		Formula distribution	Distribution of R. F. C. excess of $2,620,250		New allocations		Formula distribution	Deduct for foregoing increases in first-mortgage bonds	New allocations			
			Earnings		Bonds	Approximate	Final			Approximate	Final		
			Amount	Percent									
Rio Grande Western first-trust 4's	$20,050,800	13,634,544 (68%)	$866,190	43.2	$1,131,948	$14,766,492	$14,737,338 (73.5%)	$6,416,256 (32%)	$1,131,948	$5,284,308	$5,313,462 (26.5%)		
Rio Grande Western consolidated 4's	20,056,400							4,011,280 (20%)			4,011,280 (20%)	$14,641,172 (73%)	$1,403,948 (7%)
Junction first 5's	2,758,333	1,958,416 (71%)	126,362	6.3	165,076	2,123,492	2,123,916 (77.0%)	799,917 (29%)	165,076	634,841	634,417 (23.0%)		
Denver & Rio Grande consolidated 4's	45,727,500	10,090,950 (22%)	754,995	37.7	828,101	10,588,151	10,883,145 (23.8%)	8,239,950 (18%)	828,101	7,402,849	7,407,855 (16.2%)	10,974,600 (24%)	16,461,900 (36%)
Denver & Rio Grande consolidated 4½'s	8,823,115	1,941,085 (22%)			159,733	2,100,818	2,099,301 (23.8%)	1,588,161 (18%)	159,733	1,428,428	1,429,945 (16.2%)	2,117,548 (24%)	3,176,321 (36%)
Refunding and improvement 5's	16,950,000	2,712,000 (16%)	236,880	12.8	285,083	2,997,083	3,000,150 (17.7%)	2,203,300 (13%)	285,083	1,918,412	1,915,350 (11.3%)	3,729,000 (22%)	8,305,500 (49%)
Refunding and improvement 6's	2,990,000	478,400 (16%)			50,309	528,709	529,230 (17.7%)	388,700 (13%)	50,309	338,391	337,870 (11.3%)	657,800 (22%)	1,465,100 (49%)
Subtotal				100.0	2,620,250				2,620,250				
General mortgage 5's	33,548,155												4,354,816 (10%)
R. F. C. claim	13,900,605	7,820,220 (56%)			2,620,250		5,200,000	6,165,342 (44%)	2,620,250	3,785,582	8,703,605		
Total							38,573,680				29,750,184	32,120,120	35,167,585

United States District Court

DISTRICT OF COLORADO

Filed Oct. 25, 1943.
G. WALTER BOWMAN,
Clerk.

In the Matter of
THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *Debtor.* } No. 8669

OPINION
APPROVING PLAN OF REORGANIZATION

The Denver and Rio Grande Western Railroad Company, as debtor, and the Denver and Salt Lake Western Railroad Company, as secondary debtor, filed November 1, 1935, petitions in this court alleging they were unable to pay their debts as they matured, and desired to effect a plan of reorganization under §77 of the Act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. On the same day the petitions were filed the court entered orders approving the petitions as properly filed, and authorized and directed the debtor to operate and maintain both properties under the supervision of the court.

On November 18, 1935, Wilson McCarthy and Henry Swan were appointed Trustees for the debtor. These appointments were ratified by Division 4 of the Interstate Commerce Commission. On December 18, 1935, the court appointed Raymond L. Sauter, Trustee of the secondary debtor, The Denver and Salt Lake Western Railroad Company. This appointment was ratified by the Interstate Commerce Commission. He resigned April 21, 1941 and H. Allyn Hicks, Jr., was appointed as his successor June 13, 1941. April 29, 1936, upon petition of the debtor, an order was made extending the time for filing a plan of reorganization under §77 (d) to and including August 1, 1936. On July 29, 1936, a proposed plan of consolidation and reorganization, as of January 1, 1937, was filed with the court and the Interstate Commerce Commission by the debtor. This plan included the Denver and Rio Grande Western, the Salt Lake Western, the Denver and Salt Lake Railway Company (the Moffat Road), the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company.

Public hearings on the plan began and were held before the Interstate Commerce Commission in October, 1936, and in February, April, and June, 1937. On June 15, 1937, a plan of reorganization, including the companies covered by the debtor's plan, was filed by the so-called "Insurance Group Committee," intervener, of which George S. Van Schaick was chairman. In addition to this group other intervenors included the trustees under certain mortgages, the Security Research Bureau, the Untermyer family, Chase National Bank of New York, the Railroad Credit Corporation, various chambers of commerce and boards of trade, the Reconstruction Finance Corporation and others.

By report and order of July 11, 1939, (233 I. C. C. 515) the Commission approved a plan of reorganization for the Denver and Rio Grande Western Railroad Company and the Denver and Salt Lake Western Railroad Company, secondary debtor, The Denver and Salt Lake Railway Company, the Rio Grande Junction Railway Company and the Goshen Valley Railroad Company. Thereafter, on September 1, 1939, petitions for modification of the approved plan were filed by the so-called Insurance Group Committee, by Guy A. Thompson, Trustee of the Missouri Pacific Railroad Company, and many other interested parties.

Thereafter the Commission, having reconsidered its prior report and order, came to the conclusion that certain provisions of the plan should be modified and certain other provisions, as to which some question had been raised, should be retained without change. And on April 2, 1940, the Commission entered an order setting forth and approving a modified plan of reorganization for the Denver and Rio Grande Western Railroad Company and the Denver and Salt Lake Western Railroad Company, effective June 30, 1938, and revoking and superseding the order of July 11, 1939 (239 I. C. C. 583).

This order having been certified and filed in the court on April 11, 1940, on May 6, 1940 it was ordered all parties in interest file their objections to the plan of the Commission and their claims, if any, for equitable treatment on or before July 1, 1940, and set said objections and claims for equitable treatment for hearing on Monday, July 29, 1940.

Accordingly the matter came before this court July 29, 1940, for hearing upon the specific written objections to the plan and claims for equitable treatment (Tit. 11, §205, subdivision (e), U. S. C. A.). Testimony was taken up to August 12, 1940, at the conclusion of which, and before argument, at the suggestion of counsel, an informal conference with counsel was held in the court chambers, and at the request of counsel the court indicated

its views as to certain features for a proper plan of reorganization. (see interim memorandum of August 30, 1940), stating therein that any plan approved by the court should be within the framework of the Interstate Commerce Commission plan; that it strongly favored the consolidation of the Salt Lake and the Denver—which all the testimony supported—and setting out other requirements of any plan the court would approve, and emphasizing that the amount of fixed charges in any plan the court would approve was that fixed by the Interstate Commerce Commission, to wit, $29,403,144 of fixed interest first mortgage bonds, total fixed charges $1,278,539.

As to the allocation of the first mortgage bonds, the court indicated the three divisional mortgages, i. e., Rio Grande Western First Trust 4s, Rio Grande Junction First 5s and part of the Denver and Rio Grande Consolidated 4s and 4½s,

> "should share in the new fixed interest first mortgage bonds with the Reconstruction Finance Corporation notes on such a proportional basis as the Rio Grande Junction rate of bonded indebtedness per mile for each of such mileage, thereby awarding new fixed interest first mortgage 4s to these three divisional first mortgages, and to the Reconstruction Finance Corporation notes."

This allocation of first mortgage bonds, differing from the Interstate Commerce Commission plan, was based on traffic density between Dotsero and Salt Lake City. It is recognized that the Rio Grande Junction 5s cover sixty miles of track running from Rifle to Grand Junction, which produces substantially no local business, and the system could afford, if necessary, to turn it over to its bondholders and duplicate this mileage with a better and straighter line at a cost of less than $3,000,000. In addition, the mileage between Dotsero and Salt Lake City covered by these mortgages is dependent upon the system as a whole for equipment, terminal facilities, shops and overhead organization and personnel.

After the hearing on the Commission's report and order of April 2, 1940, above referred to, and on March 6, 1941, the court filed its opinion disapproving the Commission's plan largely for the reasons just stated, and on the same date entered its order referring the proceedings back to the Commission under Section 77 (e). In its opinion the court suggested a plan which became known as the "Court Plan." Thereafter further hearings occurred before the Commission and on July 13, 1942, it promulgated its second supplemental report and order wherein it, in effect, revoked its prior orders and substituted its said second supplemental report and

order (254 I. C. C. 5). To this, various petitions for modifications were filed with the Commission, and on June 14, 1943, it promulgated its third supplemental report and order further modifying its prior order of July 13, 1942, and as so modified, approving the same (254 I. C. C. 349).

The matter is now before the court for approval or disapproval of the Commission's plan culminating in its said third supplemental report and order of June 14, 1943, modifying its prior reports and orders. Reference to the hearing thereon before the court will be made later herein.

Railroad transportation has been a sick industry. Whether the capital burden imposed upon them has played a causative role in their maladies, or has become excessive only by reason of weakness induced by other causes, it is clear that many carriers can face the competition and other hazards of the future only if their capital charges are drastically reduced. For many, therefore, reorganization on a considerable scale was long ago indicated. Thirty per cent of the mileage of American railroads has already been subject to this process.

When most of the railroads were built—preceding 1850—financing was usually accomplished by sale of capital stock—rarely by mortgage. Underestimation of original cost was the chief source of later financial difficulties. This led to the use of the corporate mortgage necessary to finish construction, and in the era following 1850 the law and technique of corporate reorganization had its real beginning and the mortgage was used with an increasingly lavish hand. This led to the modern equity reorganization, involving the foreclosure and sale of the carrier's property to a new company formed to take it over.

Sec. 77 of the New Bankruptcy Act provides for the reorganization in the Federal courts of insolvent interstate railroads unable to meet their debts as they matured. An elaborate procedure is set out in the statute. The new statute was designed to provide a method to avoid the undue delay and inordinate costs incident to the old equity reorganization, and adoption of a fair, equitable and financially sound plan, surrounded by administrative and judicial safeguards, thought to be lacking in the equity process.

No plan can become effective without the prior approval of the Interstate Commerce Commission and the court, and they must first make a finding it is equitable, does not discriminate unfairly in favor of any class of creditors or stockholders, is financially feasible, and in the public interest. The plan must be accepted by two-thirds majority of any class of creditors or stockholders before it becomes binding upon the remainder of the class. It further

provides that the consent of any class of creditors or stockholders could be dispensed with where (1), the plan provided for the payment in cash of the value of the claim, or the value of the securities allocated under the plan to any interest in the old company. Or (2), where provision was made in the reorganization plan for a sale of the debtor's property to the reorganized company at a price not less than that to be fixed by the Interstate Commerce Commission (§77b). Shareholder approval can also be dispensed with, where it is established that their equity in the enterprise is gone. And bondholders' acceptance is unnecessary where the reorganization plan provided for the sale of the debtor's property, subject to their liens. Sec. 77 (e) of the Bankruptcy Act (Tit. 11, U. S. C. A., §205).

The amendments of 1935, while changing almost the entire language, retained the underlying concepts of §77. By it stockholders' consent is made unnecessary where the company is found to be insolvent; that is, where the value of its assets was less than its total debts. The Commission, as well as this court, has on several occasions found—and the court now finds—that the debtor is insolvent and there is no equity to justify the issuance of any securities to the stockholders of the debtor. And it is further provided that readjustment may become binding on the dissenting classes of creditors and stockholders in the event the court finds after a hearing that the plan makes provision for appraisal of their interests and cash payment of the value thereof. And where the court finds after hearing that the plan makes adequate provision for objectors' interests, their rejection of the approved plan of securities readjustment is not reasonably justified.

This railroad reorganization process of §77 has, over many years, accomplished a long step towards sound, fair, and equitable reorganizations. Like all new legislation, however, experience has developed some deficiencies. Out of the many controversies over the Act and its meaning it has been made clear that a §77 reorganization must meet the requirements of the *Boyd case*, 288 U. S. 482. In three recent cases, *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, and *Los Angeles Lumber Products Co.*, 308 U. S. 106, the Supreme Court has cleared up many disputed questions.

A reading of these cases forces the conclusion that the drafting and formulation of a sound reorganization plan is a most difficult job, especially when, as here, there are overlapping divisional mortgages and liens. It is well to observe that in twelve out of the first eighteen reorganizations before the Commission that have reached final report the common stock was found to be valueless.

In two, the Kansas, Kaw Valley & Western, and the debtor's amended plan of January 1, 1939 in the New Haven case, the debtor's plans themselves actually provided stockholders be given nothing.

Fixed charges can not be too high in relation to earning power. Neither can they be too low, because securities carrying a return which is not fixed, require a higher coupon rate. Earning power, as the Supreme Court has held *(supra)*, must obviously be the determining factor in arriving at the amount of securities the debtor can support. The main objective of a sound plan of reorganization is the determination of the future net earning power of the property and the amount of new securities such earnings will conservatively support over good and bad years alike.

For the last ten years the total consolidated net earnings available for interest on the Rio Grande and the Salt Lake—1933 to 1942, inclusive— were $43,157,877, 80% of which is $34,526,302—an average of $3,452,630 per year. This includes, of course, the inflated earnings for 1942 of $18,144,032—three times the net earnings for any single year of the ten. Comparing this with the fixed charges called for by the plan now before the court providing for total fixed charges of $1,694,941, compared with $1,766,966 called for in the 1942 plan, and $2,637,552 fixed charges provided for in the court plan of 1941. All this on the basis of consolidation with the Salt Lake. It would thus seem that on a conservative basis the prospective earnings determined as near as can be, justify the present plan.

As a commentary on the past reorganizations it is interesting to note that before the 1924 reorganization the total capitalization of the Denver and Rio Grande Western, including common and preferred stock, was $193,764,582, and at the conclusion of the reorganization the capitalization of the new company was $208,480,786—an increase rather than a decrease. With this experience the court, like a burned child, dreads the fire.

The *Western Pacific case (supra)*, held, 318 U. S. 472:

> "The power of the court does not extend to participation in all responsibilities of the Commission. Valuation is a function limited to the Commission, without the necessity of approval by the court." Sec. 77 (e), (Tit. 11, U. S. C. A., §205).

And:

> "The function of valuation thus left to the Commission is the determination of the worth of the property valued, whether stated in dollars, in securities or otherwise. * * *. None of the findings required of the judge under subsection (e) relate

specifically to valuation * * *. It leaves open the question of whether, in reaching the result the Commission had applied improper statutory standards."

The same case also held that the determination of whether the plan is "compatible with the public interest" (subsection (d) of §77 of the Bankruptcy Act (Tit. 11, U. S. C. A., §205), likewise rests with the Commission. This phrase includes, according to the Supreme Court, questions as to the amount and character of the capitalization, and 318 U. S. 474:

"So long as legal standards are followed, the judgment of the Commission on such capitalization is final."

The Supreme Court also held (syllabus No. 7):

"Section 77 (e) authorized the elimination from participation in the reorganization of stockholders and creditors whose claims are valueless."

And their elimination

"does not deprive such claimants of property without due process of law."

Further (syllabus No. 8), that nothing in the Act

"requires the issuance of warrants to stockholders and creditors whose claims, found to be without value, have been eliminated from participation in the reorganization."

And (syllabus No. 9):

"The mere possibility that earnings of the reorganized railroad may exceed expectations does not justify the issue of securities based upon such a possibility."

And further (syllabus No. 15):

"Sound railroad reorganization requires consideration of the interest of the public in an adequate, transportation system, properly financed, and this must be balanced against the satisfaction of claims, without equity, by the issue of securities without reasonable opportunities to earn a return."

Further, that a showing made before the district court as to changed conditions, to wit, increased earnings due to the war, forms no basis for rejection of the Commission's plan.

In this connection it should be stated in regard to inflated war earnings, that the passenger traffic on this property for the twelve months ending August 31, 1943 equaled $9,255,631, of which $5,536,307—or 59%—is the result of transportation of soldiers for the Government. This does not include soldiers traveling on fur-

lough or on personal account nor other passenger traffic directly due to the war such as the families of soldiers in the service going to and from camps or of representatives of Government departments incidental to the war.

Freight earnings for the 12 months ending August 31, 1943 were $57,702,824. It is difficult, if not impossible, to determine just what part of these freight earnings are due to the war effort. During the 12 months ending in August, total loadings and receipts from connections were 514,520 cars. This included 138,884 carloads consigned to various Government agencies, but does not include business moving to contractors doing Government work, nor to or from war industries operated independently, such as the so-called "Kaiser Operations," or the Colorado Fuel & Iron Company. The representatives of the Traffic Department estimate that between 60% and 70% of the present freight traffic is due to the war effort.

It would, therefore, seem that very little, if any, of these inflated earnings are sufficiently permanent to form a basis for additional securities.

In the *Milwaukee case (supra)*, the court (318 U. S. 536), sustained the Commission's conclusion that the equity of the holders of debtor's preferred and common stock was without value, and they were, therefore, not entitled to participate in the reorganization.

And (p. 541): If there was no reasonable probability that the earning power of the road would be sufficient to pay prior claims of interest and principal and leave some surplus for the service of stock, then the inclusion of stock would violate the full priority rule incorporated in §77 by the phrase "fair and equitable." Page 540: Earning power is the primary criterion of value in reorganization proceedings. Page 543: Earning power in war years is not a reliable criterion for the indefinite future. And (pp. 544 and 545): The nature of the capital structure, and the amount of the capitalization, is for the determination of the Commission, and all questions of ratio of debt to stock, the amount of fixed, as distinguished from contingent interest, and the kind of capital structure which a particular company may need to survive, are for the expert judgment of the Commission which the courts must respect. Page 566:

> "Whether in a given case senior creditors have been made whole or received 'full compensatory treatment' rests in the informed judgment of the Commission and the District Court on consideration of all relevant facts."

In *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, it was held (p. 115), that creditors are entitled to absolute priority over stockholders against the property of an insolvent corporation —relative priority not being sufficient.

When the court took over the property on November 1, 1935, and appointed Trustees, the physical condition of the estate was very bad. The management, in order to pay past due interest on outstanding securities, had not only used funds that should have been devoted to proper maintenance, but had actually borrowed money from the Reconstruction Finance Corporation to pay interest on funded debt, and current taxes as well. As a result a great deal of deferred maintenance had been allowed to accumulate. It is hard to understand the policy of the Reconstruction Finance Corporation in loaning money to this debtor for such purposes and thereby postponing and making worse the inevitable bankruptcy. The road was in such shape that on many sections of the main line trains were run on "slow orders." There was lack of protection of the roadbed and bridges on streams adjacent thereto, the rolling stock was in bad shape, all motive power was in need of repair, and the shops lacked adequate equipment.

The Trustees promptly drew up an improvement program and prosecuted it at a cost through and including the first half of 1943 of roughly $40,000,000. This includes $1,065,000 for the installation of centralized traffic control on 115 miles of the main line—mostly west of Dotsero. The net result of this alone was to enable the road to give an operation efficiency on a single track equal to about 90% of what could have been accomplished on a double track operation. $104,000 was spent on automatic block signals on the Salt Lake Western between Bond and Dotsero, and new slag ballast installed on 413 miles of roadbed, and 436 miles of new rail was laid at a cost of $6,968,500. Main terminals and freight yards were enlarged and improved at a cost of over $1,700,000. In addition many line and grade changes were made, passing tracks installed at various points, and a considerable amount of roadway and work equipment acquired.

The rehabilitation of the equipment included the purchase of six Diesel freight locomotives at a cost of $3,018,928; 23 Diesel switching locomotives $1,450,318; 20 new steam locomotives $3,759,757. In addition the Trustees purchased eight second-hand locomotives, and have five additional locomotives on lease from Defense Corporation, and have on order six more Diesel freight locomotives for delivery early in 1944.

To handle properly the present volume of business offered, further additional equipment, including motive power is required,

which can not now be obtained. The economy of Diesel operation is recognized in railroad circles, and it is the prediction of operating officials that Diesel power will supplant steam on American Railways after the war as soon as the necessary equipment can be made available. It is especially adapted to railroads running through mountainous territory with heavy grades. In addition the Trustees purchased 100 ballast, 1902 box cars, 100 automobile box cars and 791 gondola cars, including coal cars. To finance these improvements the Trustees borrowed on Trustees Certificates. $7,245,000. The first issue of these Certificates—Series D—carried an interest rate of 3¼% and the last—Series I—were sold on a 2% basis. Of this amount $1,970,000 was paid at maturity, leaving $5,275,000 outstanding in September, 1943, which the Trustees have offered to pay off without success. In addition a debt of $2,687,689 incurred under conditional sale agreements has been paid off before maturity together with the note due the Railroad Credit Corporation in the amount of $261,847. Furthermore, Series A, B, and C Equipment Trust Certificates, amounting to $2,325,000 outstanding when the Trustees took over, have been paid off. These particular Equipment Trust Certificates bore an interest rate of from 4½% to 5½%, compared with the 2% rate on the Trustees' certificates. This indicates the greatly improved credit rating the property established in banking circles under Trusteeship.

These improvements—often made over the objections of the bondholders and creditors—were justified, for otherwise the property could not have begun to handle the increased volume of traffic resulting from the war effort. As an example, the average freight train speed on this road increased steadily until in 1941, for the first time, at least since 1920, the year's average speed on the Rio Grande was faster than the average for the nation's railroads as a whole. It has not been possible, however, to maintain this rapid service even with increased facilities, taxed as the system is under wartime conditions. Yet it is noteworthy that this property in 1943 is demonstrating its ability to produce more than twice as many gross ton miles as in 1929—the heaviest year prior to Trusteeship—with a train speed 20% faster than in that year.

The opening of the Dotsero Cutoff, saving 175 miles between Denver and Salt Lake and Ogden, and the improvements made during the Trusteeship, placed the property for the first time in a competitive position with other transcontinental carriers enabling it to participate in through business with schedules on a par with other transcontinental carriers.

No material change has been made in the 146-hour basic schedule established by the transcontinental lines for eastbound freight.

from the Coast to Chicago. This required the Rio Grande to move trains from Ogden to Denver and Pueblo in 30 hours and 17 minutes. As a result of the war and the request of the Office of Defense Transportation, in 1942 this eastbound schedule was lengthened 24 hours between California and Chicago, increasing the Rio Grande schedule to 35 hours 15 minutes. Prior to 1936 the agreed westbound freight schedule from Chicago to the Pacific Coast called for seventh morning delivery. The Rio Grande's part of this schedule was 35 hours from Pueblo to Ogden, and 35 hours from Denver to Ogden. In 1936 this westbound schedule was reduced to provide for a sixth morning delivery from Chicago. This required the Rio Grande to make the run from Denver to Ogden in 26 hours, and from Pueblo in 27 hours and 30 minutes. This schedule remained in effect until November, 1941, when it went back to the seventh morning delivery.

The road runs through mountainous territory and along many streams subject to periodic floods, and there is constant danger of falling rocks and slides. This hazard has necessitated the installation of protective measures against accidents resulting from rock on the track, etc., involving constant expenditure to maintain bridges and roadbeds through deep canons, where flood conditions regularly prevail during certain times of the year. For these reasons the hope is expressed that when the railroad is taken back by its owners that the balance of the Trustees' improvement work in these respects will be carried out.

The Moffat Tunnel and the Cutoff carry more than twice as much traffic as they were originally designed for, and central traffic control on that line is strongly indicated. Smoke conditions in the Tunnel are very bad and present a problem that must be solved in the near future, either by the exclusive use of Diesel engines or the installation of some form of electric power between Denver and Bond.

This recitation of the improvement in the condition of the property between the appointment of the Trustees and this hearing bears out the experience of the court with this property in four receiverships—two of the four under my incumbency as Judge. Each time the property has been taken over by the court in a very bad condition physically, with a large amount of deferred maintenance, lack of sufficient power and rolling stock, and each time it has left the court in A-1 condition, and capable of performing its duty as a public carrier.

The Rio Grande Railroad is the largest business enterprise in Colorado, and the largest taxpayer, and also gives a very large service to the State of Utah, and the hope is expressed that when

the property is returned to the security holders they will realize their responsibility as the owners of a public utility that contributes so much to the prosperity and well-being of the states and communities it serves. The losses they have suffered in these various reorganizations can be directly traced to the security holders' failure to recognize this responsibility, and their lack of interest in their investment and its management. They have tolerated a management of their property between recurring receiverships that has resulted in failure to make earnings sufficient to maintain the overcapitalized financial structures. Failure to realize this responsibility will inevitably result in a form of reorganization carried out by a bureau of the Government less sympathetic to the owners of the property, resulting in a far greater scaling down of the capital structure than is now required by §77.

The new management of the property should be made up of Western men familiar with the problems of the customers living in the territory served by the railroad. Its control as in the past should not be centered in a group of financial institutions in New York City, the officers of which have never willingly ventured west of the Hudson River, and who set foot for the first time on their property when invited on an inspection trip by the Trustees.

This proceeding has been pending in this court approximately eight years. As already stated, the Commission's plan of April 2, 1940, certified to the court, was rejected because of its failure to give due recognition to the Rio Grande Western First Trust 4s and the Junction 5s, as compared with the Reconstruction Finance Corporation notes; and the court at that time in referring the proceedings back to the Commission, outlined a plan embodying the court's views, dated March 6, 1941. The plan now before the court bears more resemblance to the court plan than to the one first put out by the Commission.

This plan was set for hearing before the court on September 13, 1943, pursuant to notice. On April 13, 1943, the court heard, upon notice to all parties, the petition of the Trustee of the Denver and Salt Lake Western, filed March 25, 1936, as amended April 27, 1936, for payment of rental and other amounts by the Denver and Rio Grande Western Railroad Company, and upon the supplemental petition for payment of rental for the Denver and Salt Lake Western Railroad Company properties, filed February 8, 1943, and the petition of the Moffat Tunnel Improvement District in support of said petitions of the Trustee of the Salt Lake Western.

The court, after hearing testimony and arguments entered its findings, order and decree on September 13, 1943, confirming the joint trackage agreement between the Denver and Salt Lake Rail-

way Company and the Rio Grande, dated October 15, 1928, and the Dotsero Cutoff agreement between the Denver and Salt Lake Railway Company, the Salt Lake Western, and the Denver and Rio Grande, dated June 22, 1931, as modified by a subsequent agreement between the Rio Grande and the Reconstruction Finance Corporation, fixing the rental as therein provided.

It was further ordered, pursuant to the findings made, that the Rio Grande or its Trustees were not obligated to pay the Salt Lake Western as rental for the use of the Dotsero Cutoff either the interest on the principal obligation of the Salt Lake Western or the Rio Grande under the so-called stock purchase loan agreement of December 19, 1934, any Federal or state income taxes, excess profit taxes or other taxes levied upon the income of the Salt Lake Western. And further ordered the Trustees of the debtor Rio Grande to perform and to continue to perform the obligations of the Rio Grande contained in said leases and agreements and pay the rent due to date with interest and in the future.

On June 23, 1943, the Central Hanover Bank and Trust Company, Trustee under the first mortgage of the Rio Grande Junction Railway Company, dated December 1, 1889, filed its petition dated June 14, 1943, asking the court to require the debtor to pay to the Rio Grande Junction Company, for application upon the Junction bonds the principal amount of said bonds, together with interest thereon, from June 1, 1935 to date. The matter was duly noticed for hearing on June 28, 1943, and on June 23, 1943, on motion for continuance, the hearing was by request and consent of all the parties in interest including the Chase National Bank of the City of New York, as Trustee under the Denver and Rio Grande Western Railroad Company Refunding and Improvement Mortgage, continued to meet the convenience of New York counsel until September 13, 1943.

After a discussion of the status of the Junction, the Commission said in its third supplemental report of June 14, 1943 (254 I. C. C. on 363):

> "In order to prevent failure of consummation of our entire plan, however, if there is delay in disposition of the Junction affairs, or to prevent holding up the plan pending extended reorganization proceedings for that company, the plan will provide that, in the event it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan with respect to the other debtor properties, the provisions for the Junction bondholders may be considered wholly separable, and the remainder of the

plan consummated immediately. Under these circumstances, the Junction stock and lease would become assets of the reorganized company subject to the liens of its mortgages with provision for release in the event the consolidation is carried out, and the plan will provide for disaffirmance of the Junction lease in the discretion of the reorganization managers of the principal debtor and the judge."

And substantially the same statement is contained in its order (254 I. C. C. on 386) which order also provides (254 I. C. C. on 404):

"* * * The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively."

The Commission's plan allocates to holders of the Junction Company's First Mortgage Bonds 77% of their claim in first mortgage bonds on the reorganized company, and 23% in its income bonds. The outstanding problem with respect to the Junction is that it is not in trusteeship and the trustee under its First mortgage and certain bondholders have contended that the Commission had no power to allocate new securities in lieu of the first mortgage bonds or to compel acceptance thereof by the bondholders.

To the court solution of the problem seemed very simple. The trustees having on hand an amount of cash far in excess of the needs of the reorganization expenses, including working capital, and taking into account debtor's guaranty of the payment of the bonds with interest, considers the question as a matter of ordinary administration of the property, and having the old-fashioned, perhaps, feeling that this excess cash should be used to reduce indebtedness when possible, ordered the trustees to purchase the Junction bonds at 100% and interest, or pay them off, whichever seemed the most advantageous.

Accordingly and on September 16, 1943, the court entered an order directing the trustees to purchase the Junction bonds at par and accrued interest at 5% per annum, from June 1, 1935, from all bondholders tendering their bonds for purchase and the trustees have given notice pursuant to the order that on and after November 1, 1943, they will purchase such bonds at said price, but with accrued interest terminating on that date.

In view of the above quoted statements in the Commission's plan and order the court has felt justified and authorized in providing

for such purchase as not inconsistent with the plan. Disposition of the purchased bonds can later be determined by the reorganization committee and the court. They may be canceled or they may be utilized under the plan in acquisition of new securities which will become an asset of the reorganized company.

The court then took up the objections to the plan filed by most all interested parties, none of which were seriously pressed at the hearing (the Insurance Group Committee, typewritten record, p. 17; the Chase Bank, p. 22; the Untermyer Group—see objections; the Reconstruction Finance Corporation, pp. 17 and 18, and the Guaranty Trust Company, p. 19), counsel urging the approval of the plan in open court, reserving, however, the right to press their objections in detail if it was not approved by the court. The Central Hanover Bank and Trust Company, as Trustee under the first mortgage on the Rio Grande Junction Railway filed objections, mostly based upon the treatment the plan accorded the Junction bonds. These objections were eliminated, we assume, when the court granted their petition asking the Trustees be directed to purchase the Junction bonds 100% in cash, with interest.

The court has expressed its views on the various plans many times. (See Interim Memorandums August 30, 1940, December 6, 1940, March 6, 1941, August 14, 1943.)[1]

Furthermore, most of the objections made, and all those urged at the hearing, were passed upon by the Interstate Commerce Commission, whose decisions on the question involved this court must follow under the *Milwaukee* and *Western Pacific cases*, 318 U. S., so a brief reference to the plan now under consideration is all that seems necessary.

Three plans have been proposed by the Interstate Commerce Commission after hearings—all as required by §77. The first called "The Commission Plan," contained in its original report dated July 11, 1939 (233 I. C. C. 515); the second plan, set out in its report on further consideration, dated April 2, 1940 (239 I. C. C. 583); second supplemental report dated July 13, 1942 (254 I. C. C. 5); and the third supplemental report and order of June 14, 1943, certified to this court by the Commission on June 28, 1943 (254 I. C. C. 349). The last is called Approved Modified Plan on the Basis of Consolidation with the Denver and Salt Lake, with an Alternative Approved Modified Plan, without Consolidation with the Denver and Salt Lake.

The provision in former plans for an immediate loan of $2,250,000 is eliminated as unnecessary and on the basis of consolidation

[1] These four interim memorandums are not printed herein.

with the Denver and Salt Lake, the total capitalization proposed is $155,173,127, as compared with $154,521,612 previously. Annual charges are: Fixed interest $1,694,941, instead of $6,381,921.29 before this Trusteeship. Prior contingent interest $498,318, contingent interest $1,364,133, and total charges before dividends on the preferred stock $4,584,689. Other details are shown in Appendixes A and B, attached hereto.* The plan calls for $38,573,680 new first mortgage bonds, and new income bonds in the amount of $29,750,184.

The objections of Guy A. Thompson, Trustee in Bankruptcy of the Missouri Pacific Railroad Company and the debtor, the Denver and Rio Grande Western Railroad Company, may be considered together, in so far as they present any question that this court at this time can consider.

The Missouri Pacific Railroad is the owner of 150,000 shares, or one-half of the non-par common stock—the Western Pacific Railroad owning the other half—and $608,800 of the preferred stock, and $1,000,000 of refunding and improvement mortgage bonds of the debtor, the Denver and Rio Grande Railroad Company. Their chief objection is that the Interstate Commerce Commission in every plan certified to the court, finds no value or equity in the common and preferred stock of the company, and that the owners are not entitled to participate in the plan; that the plan does not preserve their interests as stockholders by providing for the issuance to stockholders of options or warrants to receive or subscribe for on fair and reasonable terms common and preferred stock in the newly-reorganized company; that the plan fails to give full and lawful effect to the value of the debtor properties and the earning power thereof past, present and prospective. Further objection is made to the alleged failure of the Commission to make a valuation of the properties of the debtor, and also that the findings of the Commission that there is no equity for the owners of the stock, is not substantiated by substantial evidence.

The same parties further alleged a large part of the traffic carried or which may be carried by the debtor railroad is and will be bridge traffic which neither originates on nor is destined for points on the Denver and Rio Grande Western Railroad Company; that a large part of it passes through the Pueblo Gateway, the volume of which is, and has been in a large measure due to the fact that the Missouri Pacific Railroad Company has been a part owner of the Rio Grande, and unless this ownership is carried forward

*Appendixes A and B are duplicates of appendixes A and B attached to Commission's third supplemental report, pages 182 and 183. They are not reprinted herein as attachments to the court's opinion.

into the new company, this long-existing channel of trade and commerce through the Pueblo Gateway over the Missouri Pacific and Rio Grande will be substantially impaired and the volume decreased, and the co-operation necessary to cause such a large volume of traffic to move thereover can be had only by ownership by the Missouri Pacific trustee of stock of the new company equal to that held by the Missouri Pacific in the old Denver and Rio Grande Western Railroad Company.

Further, that the debtor's property can not be properly operated unless the gateways of Denver and Pueblo are maintained with equal vigor; that neither the Denver nor Pueblo Gateway be impaired, and the maintenance of these two gateways be maintained. That to accomplish this, full co-operation on the part of the debtor and the Missouri Pacific Railroad is necessary but can not be brought about unless the present ownership of the Missouri Pacific Trustee in the Denver and Rio Grande Western Railroad Company is carried forward into the new company.

All of these objections, except the last in respect to the Pueblo Gateway, are fully answered and rejected in the *Western Pacific Reorganization case*, 318 U. S. 448 and the *Milwaukee Reorganization case*, 318 U. S. 532 *(supra)*. This court has found there is sufficient evidence to support the findings of the Commission, and that legal standards have been followed.

True there has been a tremendous increase in bridge traffic of the Rio Grande over a period of years. In 1920 the percentage of bridge traffic to total tonnage was 6.95%. This has steadily increased year by year until 1942, when the percentage of bridge traffic to total traffic amounted to 35.93%, out of a total tonnage of 5,496,833 tons, and for 1943 is estimated at 40% of 7,000,000 tons. Without this business this railroad could not begin to support a capital structure of any size.

For many years and until the construction of the Moffat Tunnel and the Denver and Salt Lake and the Denver and Salt Lake Western—the Cutoff—the main route of the Rio Grande was through Pueblo, where connection is made with the Missouri Pacific running to St. Louis and the East. A large volume of east and west bridge traffic has always been exchanged between the two roads at that point. I don't think it can be successfully challenged that the Missouri Pacific is equally, if not more dependent on the Rio Grande for eastbound business from the Pacific Coast delivered at Pueblo than the Rio Grande is for westbound business received from the Missouri Pacific. The Cutoff route, giving the Rio Grande a direct route from Denver to Salt Lake and the Pacific Coast—approximately 170 miles shorter than the route from Denver

through Pueblo—established another important gateway at Denver where connections are made, and a great deal of bridge traffic east and west exchanged with the Burlington, the Rock Island and the Union Pacific. This business the Rio Grande otherwise would not enjoy. It almost equals that passing through the Pueblo Gateway and does not divert any business from the Missouri Pacific at Pueblo. This short line between Denver and Salt Lake enables the Rio Grande to become a transcontinental line, competing on schedules equal to the Union Pacific on the north and the Santa Fe and Southern Pacific to the south.

The figures indicate that in 1942 the Rio Grande handled one-third less tonnage through Denver via the Moffat Tunnel Route than through Pueblo; that traffic via each route has increased in recent years. The proportion through each gateway has remained fairly constant since 1938 and while local traffic has declined in relative importance to bridge traffic, such traffic has not declined in actual tonnage. The fact is that both local and bridge traffic have shown an almost uninterrupted increase since the Trusteeship in 1935. In 1942 the Rio Grande handled 7,243,691 tons that originated on its lines, and 8,053,665 tons received from connecting carriers. In 1935 under Missouri Pacific control the property originated 4,404,574 tons of freight, and received 2,774,451 tons from other lines. The debtor's tonnage east and west through Pueblo increased 175% the total tonnage handled by the system increased 113% between 1935 and 1942 while freight originating on Class 1 railroads in the United States increased only 80% during the same period.

Passenger service from Pueblo to western and southwestern Colorado is now furnished by the Rio Grande Motor Way, and in many respects is far superior to railroad service due to more frequent as well as faster schedules. No freight train schedules through Pueblo have been canceled.

These figures indicate that under an impartial management, actuated by the best interests of the road and its customers, the Pueblo Gateway has not been hurt and demonstrates that under such a management the Missouri Pacific has exchanged more business with the Rio Grande at Pueblo during the Trusteeship than it did when it and the Western Pacific were in control. If necessary it can be shown that the Missouri Pacific control during past history of the property has been a detriment to the road and its security holders.

For these reasons the court fails to see the force of these arguments. Railroad traffic, like water, seeks its own level, and it is advantageous to both roads to exchange business at Pueblo and

maintain it as a gateway for transcontinental, or bridge traffic, irrespective of the control of one of the properties over the other.

The court is convinced from its experience with this property through two receiverships that it is for the best interests of this railroad and its security holders that it be maintained as an independent property free of control by any one road or financial group and free to make such deals with its connections as it deems fit. Reference is made to the provision of the plan under which all the voting stock of the new company both preferred and common is to be deposited in an escrow voting trust under a ten-year escrow agreement, under which either class of stock may be sold by the voting trustees subject to the approval of the Commission, and the consent of the holders of two-thirds of the escrow receipts representing the preferred and common, at a price advantageous to the interests of the new company. Under this provision control of the property can be purchased by the Missouri Pacific if it is for the best interests of the debtor.

The court has given a good deal of thought to this question during the Trusteeship, and is of the opinion that if the Missouri Pacific continues the service it maintains east from Pueblo and its splendid force of solicitors on the Coast, it will enjoy its fair proportion of the total bridge traffic moving east and west over the Rio Grande. It is not claimed, and can not be said that the Trustees have in any way favored Denver over the Pueblo Gateway. The Rio Grande is the middle link between its eastern connections both at Denver and Pueblo, and the Southern Pacific and Western Pacific at Salt Lake and Ogden, and has little opportunity to divert business from one gateway to the other.

Under the plan now before the court the Rio Grande Western first trust 4s get 73.5% of their claim in new first mortgage bonds and 26.5% in income bonds, as against 71% and 29%, respectively, under the plan rejected by the court while the Reconstruction Finance Corporation notes get 37.4% in first mortgage bonds and 62.6% in income bonds, and the Junction 5s having been purchased, the objections of the court to the former plan are in part at least corrected.

This property has gone through bankruptcy four times during its short history. These recurring financial crises in its affairs have been due in part to excessive capital structures and high fixed charges which the property has been wholly unable to earn under the management in control. In each reorganization the capital structure has not been cut to a level the earnings could support. Our experience with the property in two of these reorganizations convinces us that its financial troubles have been due in part

to absentee management wholly out of touch with the people and territory served. The court has suggested to the Commission more than once that the members of the reorganization committee and the directors of the new company should be residents of Colorado and Utah and their meetings should be held in Denver the main office of the debtor.

We have also suggested that the capital fund and depreciation fund be earmarked in cash and used only for those purposes. The Commission, however, has not accepted these views and while the court is still convinced they are for the best interests of the property and its security holders, this difference of opinion is not of sufficient importance to justify rejection of the plan.

It is suggested by competent railroad authorities that the only solution for the American railroads in the coming post-war competition is to build super-railroads to meet this competition. Great improvement in railroad plants and equipment will be required, together with many technical improvements—all at a very large cost. It involves intensive physical developments of roadbed and line, and motive power of such high capacity that maximum size freight and passenger trains can operate over long distances without intermediate speed restrictions due to adverse physical characteristics. The most modern standards of grade and curves and higher standards of design for all the components of the railroad plant must be adopted. Funds for this program must be obtained from earnings, depreciation reserves and new financing.

The court, being satisfied that the present plan complies with the provisions of subsection (b), (d), (e), of §205, Tit. 11, U. S. C. A., is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and conforms to the requirements of the law of the land regarding the participation of various classes of creditors and stockholders, and that all amounts to be paid by the debtor for expenses and fees incident to the reorganization have been fully disclosed, and provides for the payment of all costs of administration, and all allowances made or to be made by the judge, does hereby approve the plan in accordance with law.

Findings and an order in accordance herewith will be entered.

October 25, 1943.

(Printed) J. FOSTER SYMES,

District Judge.

United States District Court

FOR THE DISTRICT OF COLORADO

No. 8669

Filed Oct. 25, 1943.
G. WALTER BOWMAN,
Clerk.

In the Matter of

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *Debtor.*

In Proceedings for the Reorganization of a Railroad.

ORDER NO. 495

ORDER APPROVING PLAN OF REORGANIZATION.

These proceedings coming on for hearing on the modified plan of reorganization for The Denver and Rio Grande Western Railroad Company (hereinafter called the Debtor) and The Denver and Salt Lake Western Railroad Company (hereinafter called the subsidiary debtor), approved by the Interstate Commerce Commission (hereinafter called the Commission) in its third supplemental report and order entered June 14, 1943 (hereinafter called the Plan and certified to this Court by the Commission on June 28, 1943, together with the transcript of all the proceedings before the Commission and a copy of its said third supplemental report and order approving the plan, and the Court having considered the entire record in these proceedings, including said transcript of all proceedings before the Commission and the evidence adduced and arguments presented at the hearing before this Court beginning on September 13, 1943.

THE COURT FINDS:

1. The findings and conclusions of the Commission stated in its Original Report of July 11, 1939 (Printed Record 5047–5200), its report on further consideration dated April 2, 1940 (P. R. 5815–5881), its second supplemental report dated July 13, 1942 (P. R. 9129–9258) and its said third supplemental report and order of June 14, 1943 (P. R. 10077–10181), as to each of said reports as modified by all subsequent said reports, are supported by evidence and are correct in fact and law and are adopted as findings and

conclusions of this Court, both as to liens of mortgages and otherwise without limitation, as fully as if set out at length herein.

2. The Plan:

(a) Includes provisions modifying and altering the rights of creditors of the Debtor and the subsidiary debtor;

(b) Provides for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there will be adequate coverage of such fixed charges by the probable earnings available for the payment thereof;

(c) Provides adequate means for the execution of the plan; and

(d) In all other respects complies with the provisions of subsection (b) of Section 77 of the Bankruptcy Law, as amended.

3. The Plan:

(a) Is fair and equitable;

(b) Affords due recognition to the rights of each class of creditors and stockholders;

(c) Does not discriminate unfairly in favor of any class of of creditors or stockholders;

(d) Will conform to the requirements of the law of the land regarding the participating of the various classes of creditors and stockholders; and

(e) Provides for the payment of all costs of administration and all other allowances made or to be made by this Court.

4. (a) By Order No. 282 entered May 6, 1940 (P. R. 5930–5934) this Court required that each and every individual or corporation having or desiring to present any claim for expenses and fees incident to the reorganization herein should file such claim in the form of a petition in the office of the clerk of this Court on or before June 1, 1940 and that a copy of each such petition should be forwarded by the Clerk of this Court to the Commission for the fixing of a maximum limit with respect to the amounts to be allowed for

such expenses or fees. Petitions for such allowances were filed by numerous parties to this proceeding, such petitions generally covering the period prior to May 20, 1940, as suggested by the Bureau of Finance of the Commission in a notice sent to all parties in interest. By its Report and Order dated August 26, 1940 (P. R. 6786–6846) the Commission fixed the respective amounts stated therein as the maximum limits of final allowances to be paid out of the estate of the Debtor, as reasonable compensation for all services rendered and as reimbursement for all actual and reasonable expenses incurred by such petitioners and their counsel and technical advisers, in connection with the proceedings and plan of reorganization of the debtor to May 20, 1940, without prejudice to further allowances of fees and expenses for periods subsequent thereto upon appropriate supplemental petitions. By Order No. 333 entered April 14, 1941 (P. R. 7755) this Court made reasonable allowances within the maximum limits so fixed to certain of such petitioners, and denied allowances to others of said petitioners.

(b) By Order No. 463 entered July 1, 1943 (P. R. 10196) this Court required that each and every individual or corporation having or desiring to present any claim for compensation for services rendered or for expenses (including reasonable attorneys' fees) either under clause (12) of subsection (c) of Section 77, or otherwise, should file such claim in the form of a petition in the office of the Clerk of this Court on or before August 23, 1943, such petitions to cover all such services rendered and expenses incurred up to and including July 1, 1943; and said order further provided that a copy of each such petition should be transmitted by the Clerk of this Court to the Commission for the fixing of a maximum limit with respect to the amounts to be allowed for such compensation or expenses. Petitions for such allowances have been so filed by numerous parties to this proceeding, have been duly transmitted to the Commission, and are now pending before said Commission. No payments of compensation or expenses prayed for by said petitions shall be made by the Debtor or the subsidiary debtor or by any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor, except in such amounts as may hereafter be approved as reasonable by order of this Court within such maximum limits as shall have been fixed by the Commission. No payment of expenses or fees incident to the reorganization for the period through July 1, 1943 shall be made by the debtor, the subsidiary debtor, or any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor to any person except as prayed for in the petitions referred to in sub-paragraph (a) of this paragraph 4 or in this sub-paragraph (b) of this paragraph 4,

subject, as to the amounts prayed for in the petitions referred to in this sub-paragraph (b) to the maximum limits to be fixed by the Commission and the actual amounts to be fixed by further order of this Cou[illegible].

(c) Such additional amounts as may be required to be paid by the debtor, or the subsidiary debtor, or any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor for services performed and expenses incurred (including reasonable attorneys' fees) after July 1, 1943, in connection with the proceeding and the Plan, and in connection with the carrying out of the Plan, if it be finally confirmed, can not be ascertained at this time, but such amounts will be subject to the approval of this Court within maximum limits hereafter to be fixed by the Commission.

(d) The approximate amounts to be paid by the Debtor, or the Subsidiary Debtor, or by any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of said hearing before this Court beginning on September 13, 1943, or at the date of this Order; so far as they can be so ascertained said expenses and fees are reasonable; and said expenses and fees as to those heretofore allowed are, and as to those hereafter allowed will be, within such maximum limits as are fixed by the Commission, and within the maximum limits so fixed have been or are to be subject to the approval of this Court.

5. By Order No. 95 entered November 23, 1936 (P. R. 2146–52) this Court divided the creditors and stockholders of the debtor and the subsidiary debtor into classes.

6. This Court has jurisdiction of the subject matter of these proceedings and of the debtor and the subsidiary debtor and their respective properties, creditors and stockholders, and all other parties having claims against or interest in the debtor or the subsidiary debtor or its or their property.

7. The foregoing findings shall be taken and deemed to be findings of fact, and in addition, to the extent appropriate, conclusions of law and also orders.

WHEREFORE, IT IS ORDERED:

FIRST: All objections heretofore filed herein to the Plan, and all claims heretofore filed herein for equitable treatment otherwise than through the Plan, are hereby severally overruled and denied

and the motions to remand the Plan to the Commission and to dismiss the proceedings are hereby severally overruled and denied.

SECOND: The Plan is hereby in all respects approved.

THIRD: The finding made by the Commission (P. R. 10143) that the interest of the holders of equipment obligations of the Debtor, equipment trust certificates of the Trustees and any other obligations under equipment leases or sales agreements will not be adversely and materially affected by the Plan is hereby affirmed.

FOURTH: The finding of the Commission (P. R. 5164 and 10175) that claims against the Debtors and their subsidiaries entitled to priority over their respective mortgages, claims for taxes levied, assessed or accrued against the Debtors, their subsidiaries or trustees, current liabilities and obligations incurred by the Trustees during the reorganization proceedings and claims arising from disaffirmance of executory leases or contracts of the Trustees pursuant to orders of the Court, in respect of which claims are filed or evidenced in accordance with orders of the Court, and the interests of parties to agreements and executory contracts with the Debtors assumed by the reorganized company, are not adversely and materially affected by the Plan is hereby affirmed.

FIFTH: The finding of the Commission (P. R. 10169) that the interests or equities of (1) all general unsecured creditors of the Debtor whose claims are not entitled to priority over the mortgages of the Debtor, (2) holders of preferred stock of the Debtor and (3) holders of common stock of the Debtor, have no value and nothing shall be distributable to them is hereby affirmed.

SIXTH: The Court reserves full jurisdiction to construe the Plan, to cure any defect, supply any omission and reconcile any inconsistency in the plan and to exercise all its powers under the Plan, all in such manner and to such extent as may be necessary or expedient to carry out the Plan effectively.

Dated October 25th, 1943.

(Printed) J. FOSTER SYMES,

U. S. District Judge.

A True Copy Teste

G. WALTER BOWMAN, *Clerk.*

By WILLIAM GRAF, *Deputy Clerk.*

[fol. 212]

MEMORANDUM ON CONFIRMATION OF PLAN—Filed November 1, 1944

By order of March 23, 1944 the Interstate Commerce Commission on April 26, 1944, submitted for acceptance or rejection by creditors of Classes 6, 7, 8, 10a, 10b and 11, 12a and 12b of the Denver & Rio Grande Western Railroad Company, the above debtor, and by creditors of Classes 1 and 2 of the Denver & Salt Lake Western Railroad Company, as therein provided, a plan for the reorganization of the debtor, the Denver & Rio Grande Western Railroad Company and of the Denver & Salt Lake [fol. 213] Western Railroad Company—a subsidiary-debtor—approved by the Commission in its Third Supplemental Report and Order of June 14, 1943 and approved by this court October 25, 1943.

Under date of July 4, 1944 the Commission has certified to this court the results of the vote on the submission of the plan of reorganization to the creditors of the Denver & Rio Grande Western Railroad Company, debtor, et al., as aforesaid, showing that said plan had been accepted by more than two-thirds in amount of the total of such claims voting, except that creditors of Class 11, holding $1,332,050 principal amount of Denver & Rio Grande Western Railroad Company General Mortgage Bonds, constituting 20.67% of the total amount of allowed claims of said class, voted for the plan, and creditors of said class holding $5,111,100 principal amount, or 79.33% of allowed claims of that class, voted to reject the plan.

Thereafter objections to the confirmation of the plan were filed by the debtor, the Denver & Rio Grande Western Railroad Company, by Guy A. Thompson, Trustee of the Missouri Pacific Railroad Company and by the City Bank Farmers Trust Company of New York, Trustee of the General Mortgage aforesaid. Said objections were set down for, and came on for hearing on August 30th and 31st, 1944, pursuant to notice to all parties. Full argument and hearing were had. Briefs were filed on behalf of said objectors, and in reply thereto by other trustees and interested parties.

[fol. 214] The claim of the General Mortgage Bonds on the effective date of the plan aggregated $43,500,000—

about one-fourth of the debtor's entire debt. It is claimed that when the capitalization of the new company was fixed at $155,173,127 on the basis of consolidation with the Denver & Salt Lake, and $143,528,027 for the debtor alone, if consolidation is not carried out, the Commission took care of every bond issue ahead of the General Mortgage (a junior issue), for 100% of their claims in new securities, and what was left over went to the General Mortgage. At that time the so-called Junction Bonds were in the hands of the public and in the plan the Commission provided that the Rio Grande Junction 5s—whose claim amounted to $2,758,333—should receive 77% thereof in First Mortgage Bonds, $2,123,916 par, and 23% in Income Bonds, or $634,417 par, and that after all the creditors ahead of the General Mortgage bondholders were taken care of, there was only enough common stock left over to give the General mortgages 10% of their claim in par value common stock.

That thereafter the wartime earnings of the property were so large that the cash jumped from $10,000,000 to $20,000,000, or better, and counsel says the court very appropriately in September, 1943, instructed the Trustees to buy the Junction Bonds at par and accrued interest and reduced the senior debt by that amount. That by reason thereof the trustee of the General Mortgage Bonds now asks; not for any change whatever in the valuation or [fol. 215] capitalization of the debtor, but simply an adjustment such as it says the Commission authorized to be made within the framework of the plan by a redistribution of the new securities that the plan allots to the Junction Bonds, and in so doing maintain the same priority as before between the various issues. That it is simply a matter of accounting.

It is argued that in several other railroad reorganizations, that between the time the Commission put down a plan and the time it got to the court for action, the surplus cash of the respective debtors increased very much so the senior debts could be reduced. That in cases that have come down from the Interstate Commerce Commission since last September it has been said if the surplus cash is used to reduce the senior debt and stops there, for practicable purposes the capitalization of the new company is reduced below that authorized and what the Commission has found the debtor should and can reasonably

support. That the way to adjust is to take the new securities allotted to the senior bonds or debt thus paid off and redistribute them, keeping everybody's position relatively the same. That this would shove everybody up a little and give the junior issues better treatment.

It is further urged by this mortgage trustee that the reorganization committee or court should make this adjustment on the basis of the distribution the Commission has followed, and distribute the $2,758,333 bonds set aside to exchange for the Junction Bonds in the plan, keeping the same priorities.

[fol. 216] In support of this theory attention is directed to the New Haven reorganization, 54 Fed. Supp. 595 and 631. In that case there were certain first and refunding mortgage bonds up as collateral to secure six bank loans aggregating $26,000,000.

The court took $18,000,000 of surplus cash resulting from wartime earnings and with the Commission, decided they could apply it to reduce the claims of the banks by paying the accumulated interest thereon. The problem then was to make a redistribution of the $18,250,000 in bonds provided for in the plan for that purpose, and the court held it should be redistributed along the line that counsel are contending should be done here.

Judge Hincks says by paying off the accumulated interest thereon the secured claims were reduced, so that only $84,800,000 in fixed interest bonds were required, this resulting in a capital structure with a bonded indebtedness less than that which the Commission had found the railroad could reasonably support. Thus a block of $6,000,000 in fixed interest bonds and $11,680,000 in income bonds became available to sweeten the treatment previously proposed for all mortgage creditors. And this was done. Judge Hincks, however, adds that all creditors agreed that these excess securities should be distributed to all secured creditors not already awarded the full value of their claims in fixed interest bonds.

Judge Hincks then went further and paid the bank loans in full out of surplus cash and said, I quote (p. 608):

[fol. 217] "I doubt whether these conclusions require that the plan be returned to the Commission. I incline to believe that the necessary correction can be accomplished within the framework of the plan in

complete conformity with all the valid findings of the Commission."

By analogy counsel argue that in the Rio Grande situation the $2,123,916 Fixed Interest Bonds and $634,417 of Income Bonds allocated to the Junctions should be used to sweeten the treatment previously proposed for all mortgage creditors who have not already been awarded the full value of their claims in Fixed Interest Bonds.

What Judge Hincks did was to pay the bank loans off in full out of surplus cash, stating he believed this action could be accomplished by the court within the framework of the plan without returning it to the Commission, and that this action was based upon the findings of the Commission and was consistent with its limitations and within the power of the judge to make. Later the Commission filed a report approving everything Judge Hincks had done in this respect.

Judge Hincks, however, after expressing doubts whether his action required the plan be returned to the Commission stated, p. 608:

> "I incline to believe that the necessary correction can be accomplished within the framework of the plan in complete conformity with the valid findings of the Commission."

[fol. 218] In view of the sharp division between the functions of the district courts and the Commission in § 77 reorganizations announced by the Supreme Court (Ecker v. Western Pacific R. Corp., 318 U. S. 448 and Group of Investors v. Milwaukee R. Co., 318 U. S. 523), the action of Judge Hincks is hardly authority—at least until approved by an appellate court. What he really did was to make his ruling and then ask the Commission to approve.

In the final analysis, however, what Judge Hincks really did in the New Haven case was to pay off an obligation of the estate, while here the court in its treatment of the Junction Bonds did not pay off a debt, but only purchased securities, thereby giving the debtor control of another railroad property, to wit, the Rio Grande Junction Railroad Company—a necessary part of its system.

The plan itself does not contemplate the capitalization of the new company be absolutely static, but subject to

change, because it provides, as Mr. Gibson well points out (p. 10142 of the printed court record and P. 66 of the court reprint):

> "The capitalization of the new company, as of January 1, 1943, after consummation of the plan, including the merger or consolidation of the Salt Lake, shall consist substantially of the following securities, excluding those to be pledged, the amounts stated being subject to reduction to the extent, if any, that matured interest proposed to be funded in the plan is [fol. 219] paid, and as equipment obligations or other liabilities are paid or reduced, * * *."

Frankly, I do not believe the court has the power to make the reallocation requested by the General Mortgage trustee, because it would, in effect, change the allotment of every security dealt with in the plan.

Counsel argue that the court has the power asserted under 5, T, p. 105 of the printed plan, where the Commission says:

> "The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively."

The Commission, however, has no power to delegate powers or duties to the court. It is not claimed there is a defect in the plan, nor that there is any omission or inconsistency.

The modification in the Milwaukee case referred to is contained in "Summary of Second Supplemental Report of the Commission" dated December 6, 1943, and says:

> "This report approves certain adjustments of the plan of reorganization of the Chicago, Milwaukee, St. Paul & Pacific Railroad Company approved * * * June 4, 1940."

Furthermore it appears in said report that the Commission itself distributed $52,038,0[illegible] of cash on account of interest accruing during the trusteeship, not authorized [fol. 220] by the court. Next the Commission stated that in view of the payment of a bank loan and the reduction in amount of the claim of the Reconstruction Finance Corporation since the date of the plan, and the distribution

to creditors of $5,000,000 of first mortgage bonds previously set aside for new money, approximately $7,096,336 of first mortgage bonds will be issued to the Milwaukee & Northern first mortgage bondholders, Milwaukee & Northern consolidated mortgage bondholders and the debtor's general mortgage bondholders.

> "in addition to the amounts of such bonds allotted to them in the plan previously approved."

In other words the Commission itself made an allocation, which in the case at bar it is urged the court make.

Next the objectors in support of their objections complain of a too low capitalization of the new company. In view of the past history of this property it is hard for this court to take stock in any such argument. The court has attempted to dispose of it in previous opinions, and it has been rejected by the Supreme Court (infra). The permissible capitalization is a matter entirely under the jurisdiction of the Interstate Commerce Commission. Ecker v. Western Pacific R. Corp. (supra), p. 483.

In the Milwaukee case (supra), the Supreme Court said, p. 541:

> "Certainly there is no constitutional reason why earning power may not be utilized as the criterion for [fol. 221] determining value for reorganization purposes. And it is our view that Congress when it passed §77 made earning power the primary criterion."

A factor that cannot be overlooked in capitalizing earnings is the steady and material reduction in average revenue per ton mile—the basic index of the gross yield from transportation service. The average revenue of this road per ton mile declined from 1.765 cents in 1921 (Rio Grande annual report 1936, p. 27), to 0.994 cents in 1943 (annual report 1943, p. 29), a decrease of almost 50%.

Other factors which dampen optimism as to the continuation of higher earnings in the future are income taxes which this road has not been liable for since 1939, except 1942 and 1943, and very large increases in operating expenses, as shown in the Commission's 1939 report on a plan. This shows greatly increased operating costs, such as wages, fuel, materials and supplies of all kinds, and more than

offsets the economies effected by the Improvement Program. Dividends have not been paid on either class of Rio Grande stocks since 1911.

A study of the traffic gains of the railroads of the country indicates that in the third year of complete wartime prosperity the western carriers will be the most outstanding beneficiaries of the increase in railroad gross earnings. For many years before the war the western carriers suffered sharply reduced revenues, wholly inadequate to cover [fol. 222] bond interest and fixed charges. Most of the bankrupt railroads are located west of the Mississippi River.

In the early upswing of business in 1940 and 1941 the western group failed to match the operating improvement made by the eastern carriers, and it was not until 1942 that an abrupt change in operating conditions resulted in the western roads reaping the harvest of profits comparable to the gains of the eastern roads.

The reasons for this are the tremendous increase in transcontinental traffic due to the war in the Pacific, restrictions on shipping, and the closing of the Panama Canal. Also the lessening of truck competition, which in the past played havoc with the western carriers, but has largely ceased as a competitive factor since 1942. Also passenger business has returned to the railroads in large volume due to these wartime limitations on motor transportation. The Southern Pacific, for instance, shows an increase in passenger revenues from $24,000,000 in 1940 to $124,000,000 in 1943 and may reach $150,000,000 in 1944. The St. Louis & San Francisco shows an increase in passenger revenue from $3,000,000 in 1940 to $23,000,000 last year. The expected shift in war equipment to the Pacific combat area may sustain these increased earnings of western railroads for a few years after the war.

Another favorable factor is: Normally eastbound railroad traffic of the western and eastern carriers is heavier. War traffic demands have, however, brought about a diver- [fol. 223] gent shift for the two groups, and there are indications that this factor will last as long as the war with Japan. But the end to the war will undoubtedly result not only in a sharp contraction of freight tonnage but also restore the former unfavorable balance of train movements.

It is estimated that 60% of the inflated earnings of the debtor for the last three or four years is due to Government and war business both freight and passenger, but as has already been pointed out by this court, as well as the Supreme Court, war earnings are not a sufficiently stable basis for new capitalization.

Counsel refers to new industries located along the line of this debtor, but does not list them or state whether they are permanent or not. Of the few plants located along the line known as war industries, Camp Hale—a training camp at Leadville, Colorado—has been abandoned and practically no personnel left. The Kalunite plant, located in the Roper Yards outside of Salt Lake—which treats alunite ores—is still operating, but it is anticipated it will not survive the war. The Remington Arms plant at Salt Lake has been closed and is now used only as a storage depot. The activities of the Remington plant at Denver are greatly curtailed. The Kearns Replacement Center in Utah, while still fairly active will eventually be closed. Camp Carson at Colorado Springs is already greatly reduced in size. The Naval Supply Depot at Clearfield, Utah, and the Columbia Steel plant at Geneva, Utah, are [fol. 224] the only ones promising any permanency as business producers of this property.

The plan gives the old Junction Bonds $2,123,916 in the new First Mortgage Bonds and $634,417 in new Income Bonds. Under the priority rule of the Boyd case, 228 U. S. 482, in any reallotment of these senior securities they would mostly go to the First Trust 4s and the Western Consolidateds, and the so-called sweetening process would increase the General Mortgage Bonds' allotment very little, if any. The most they would get would be more common stock which has little or no value, and would only dilute the value of the common stock they now get. True they might get more stock—that is more pieces of paper—the total value of which would be little, if any more, than of that they now get.

It is said the debtor's income available for interest during trusteeship aggregated $28,700,000, which according to counsel, was used by the Trustees to carry out an improvement program, and that this expenditure is reflected in greatly increased earnings that would well support an increased capitalization.

The net operating income of this property available for interest, as restated under the plan, for the year 1941 was $3,428,000; 1940, $1,966,878; 1939, $1,235,209, and in 1938 and 1937 there was a deficit. The net after interest accruals and other charges under the new plan for 1941 was $683,082. In 1939 there was a deficit for said purpose of $502,808, and for 1938 there was a deficit of $2,172,128; in 1937 a deficit of $3,840,548.

[fol. 225] From the calendar year 1932, up to and including the calendar year 1940, there was only one year, 1933, when there was available for interest on the new Income Bonds the amount the plan calls for, and then only by disregarding the cumulative interest provision of the plan. This was at a time when every economy was practiced by the debtor at the expense of maintenance of the property. In addition this was one of the years in which money was borrowed to pay current taxes and interest not earned on the Denver & Rio Grande First Consolidated and the Rio Grande Western First Trusts.

The court in its plan of March 6, 1941 gave the General Mortgage bondholders more common stock than does the approved plan. The Commission, however, could not agree with our views, and it would seem to be a useless gesture for the court to make the same error again assuming we had the power.

A basic requirement of any reorganization, according to the Supreme Court

> "is the determination of a capitalization which makes it possible not only to respect the priorities of the various classes of claimants but also to give the new company a reasonable prospect for survival. * * * Only 'meticulous regard for earning capacity' * * * can afford the old security holders protection against a dilution of their priorities and can give the new company some safeguards against *the scourge of overcapitalization.*" (Emphasis ours.) Group of Investors v. Milwaukee R. Co. (supra), pp. 540-41.

[fol. 226] Boiling the argument down, in the final analysis it is the old one of security holders having made an unwise investment and now look to the bankruptcy court to restore values by some sleight of hand or legerdemain, which never existed or have been wiped out by mismanagement. A § 77 bankruptcy reorganization proceeding,

however, contemplates the scaling down of all claims and that the security holders may take a substantial loss. The procedure is not one designed to recoup losses.

The $25,000,000 or more the Trustees have expended in the Improvement Program inures to the benefit of the common stock. If the latter is worth anything it is as much due to these expenditures as to any other factor. This, with the increase in current assets and wartime earnings which counsel seem to believe are permanent, constitute the only equity behind the preferred and common stock.

No security holder is getting what he thinks he should. All have suffered losses. The plan is not the best imaginable—it is the only one of several that have come before the court with the practically unanimous approval of all interested parties. And in the court's opinion, any further delay or resubmission to the Commission would prejudice the successful and speedy consummation of the reorganization of this debtor and its removal from the court—a consummation devoutly desired.

For the reasons stated the court does not believe the objections under consideration are tenable, and the plan [fol. 227] having been accepted by two-thirds in amount of the total voting of the allowed claims of each class voting except the one, such acceptances not having been made or procured by any means forbidden by law the court, after full hearing, hereby finds it makes adequate provision for fair and equitable treatment for the one class of creditors rejecting it, to wit, the holders of the General Mortgage Bonds, and their rejection is not reasonably justified in the light of the respective rights, and all of the relevant facts and interests of those rejecting it. And furthermore, that it conforms with all provisions of subsection (e) of § 205, Tit. 11, U. S. C. A.

A recapitulation of the vote on the plan indicates that 40.77% of the total outstanding claims in the hands of the public voted to accept the plan, only 4.99% voted against. It would seem inequitable to reject this plan, approved, as it is, by all except a small minority of the total securities voting, especially if we consider the length of time the property has been in the hands of the court, and the exhaustive hearings on these same objections that have been had both before the Interstate Commerce Commission and this court.

But even if the petition of the City Bank were granted the so-called Insurance Group which approves this plan would, in any reallocation, receive the senior securities that the objecting trustee refers to. This because Mr. Justice Douglas in the Milwaukee opinion (supra), states that compensation must be given to the senior creditors for [fol. 228] their sacrifice of their senior position in taking junior securities, and it is only after their claim is fully satisfied that anything can be allocated to junior liens.

The General Mortgage bondholders say, in effect, that the $2,700,000 in new First Mortgage and Income Bonds thus released would go to the senior creditors; that this in turn would free an equal amount of junior securities now allotted to senior bondholders, which would, in turn, go to the second lienors, thus freeing finally the most junior securities, that is stock, to the General Mortgage Bonds. In the opinion of the court such a reallocation of securities can only be made by the Commission. The net result would be that the senior creditors would receive a larger amount of senior securities than they do now.

The only class of creditors who have failed to assent are the most junior in this picture who, as a condition of their assent, ask for an increase in the total capitalization. But, for reasons stated and authorities cited, this is a matter clearly within the power of the Commission, which has rejected the argument more than once.

As to the non-assenting classes the language of the statute is:

> "if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, [fol. 229] that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it."

And:

> "that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts."

And finally:

> "that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e)."

I am satisfied, and find after hearing, that all the requirements of the statute have been met; that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it, and it is hereby confirmed.

Proper findings and order as required may be prepared and submitted by counsel.

J. Foster Symes, District Judge.

November 1, 1944.

[File endorsement omitted.]

[fol. 230] In United States District Court

Ordering Confirming Plan of Reorganization—Filed November 29, 1944

These proceedings having come on to be heard on August 30-31, 1944, pursuant to the order of this Court entered July 20, 1944, for a consideration of the confirmation of the Modified Plan of Reorganization (hereinafter called the Plan) for The Denver and Rio Grande Western Railroad Company (hereinafter called the Debtor) and The Denver and Salt Lake Western Railroad Company (hereinafter called the Subsidiary Debtor) approved by the Interstate Commerce Commission (hereinafter called the Commission) in its Third Supplemental Report and Order entered June 14, 1943, and approved by Order of this Court entered October 25, 1943, and there being filed with the Court a certificate of the Commission dated July 4, 1944, and other data with respect to the submission of the Plan to creditors for acceptance or rejection, and evidence having been received and the Court having considered the entire record in these proceedings, including the transcript of all proceedings before the Commission, the transcript of all prior proceedings before the Court and the evidence [fol. 231] adduced and arguments presented at the hearing before the Court beginning on August 30, 1944, and being fully advised in the premises,

The Court Is Satisfied and Finds that:

1. This Court has jurisdiction of the subject matter of these proceedings and of all the parties hereto and has

jurisdiction over the Debtor and the Subsidiary Debtor and their respective properties, wherever located, and of their respective creditors and stockholders and all other persons having claims against or interests in the Debtor or the Subsidiary Debtor or its or their property.

2. This Court has heretofore approved the Plan, a copy of which is on file herein and by reference made a part hereof. On October 25, 1943, this Court filed an opinion stating its conclusions and reasons for such approval and entered an order containing the findings of this Court and approving the Plan (Order No. 495), and certified copies of said opinion and order were sent to the Commission.

3. Pursuant to an Order entered by this Court on July 17, 1936 (Order No. 69, Rec. 1575) and an Order entered by this Court on September 4, 1935 (Order No. 81, Rec. 1818), lists of all known bondholders, creditors and stockholders of the Debtor and the Subsidiary Debtor, together with other information in connection therewith in satisfaction of all requirements of Section 77 of "An Act to Establish a Uniform System of Bankruptcy Throughout the United States" as amended (hereinafter called Section 77), were prepared and filed with the Clerk of this Court on September 9, 1936 (Rec. 1929) and September 15, 1936 (Rec. 1986) and copies thereof were duly transmitted to the Commission. By request of the Commission in July, 1943, the Trustees made a comprehen- [fol. 232] sive search by examination of records, circular letters of inquiry and advertisements in various newspapers, commercial and financial journals and investment services to modernize and perfect the original lists so filed and the new lists so prepared were duly transmitted to the Commission on or about April 19, 1944, and supplemental lists were so transmitted on or about April 25, 1944.

4. On or about April 26, 1944, the Commission, in conformity with subsection (e) of Section 77 and pursuant to its said Order dated March 23, 1944, duly submitted the Plan for acceptance or rejection to the creditors of the Debtor of Classes 6, 7, 8, 10, 11 and 12 as classified by an Order entered by this Court on November 23, 1936 (Order No. 96, Rec. 2146) and to the stockholders and creditors of the Subsidiary Debtor of Classes 1 and 2 as classified

by an order entered by this Court on February 5, 1937 (Order No. 110, Rec. 2483).

5. By said Order No. 495 entered October 25, 1943, this Court affirmed the finding of the Commission that the interests or equities of (1) all general unsecured creditors of the Debtor whose claims are not entitled to priority over the mortgages of the Debtor, (2) holders of Preferred Stock of the Debtor and (3) holders of Common Stock of the Debtor, have no value. Creditors of Classes 3, 4 and 5, as classified by said Order dated November 23, 1936, and holders of claims referred to in paragraphs Third and Fourth of said Order of October 25, 1943, are not materially and adversely affected by the Plan.

6. By an Order entered September 16, 1943, this Court directed the Trustees to purchase the Junction Bonds at a price specified therein; substantially all of such bonds have been so purchased; and the Trustees, subject to further order of this Court, are hereby directed to hold the aggregate purchase price for such of said bonds as have not here-
[fol. 233] tofore been purchased in a separate account for the purpose of purchasing such bonds.

7. In view of the provisions of the Plan, the findings of the Commission contained in its Order of June 14, 1943, the findings of this Court contained in said Order of October 25, 1943, and the matters referred to in paragraph 6 hereof, submission of the Plan to any class or classes of creditors or stockholders other than those to which it was submitted as aforesaid was not required under subsection (e) of Section 77. The United States is not a creditor of the Debtor or of the Subsidiary Debtor on claims for taxes or customs duties, unless it be on claims for the payment of which the Plan duly provides and the Plan need not be submitted to the United States of America, the President of the United States, or any officer or agency designated by him.

8. The Commission by its certificate dated July 4, 1944, duly filed herein has duly certified to this Court the fact, form, method and results of such submission of the Plan for acceptance or rejection. Copies of the Commission's said Order of March 23, 1944, of the Commission's said certificate of July 4, 1944, and of the lists of creditors to whom submission was made and duplicate originals of the

ballots returned to the Commission were duly filed in this proceeding.

9. Thereafter said Order of this Court was entered on July 20, 1944, setting a hearing for the consideration of the confirmation of the Plan. Notice of such hearing was given in accordance with the provisions of said Order. The notice so given constitutes due notice to the Debtor, its Trustees, the Subsidiary Debtor, its Trustees, the stockholders and creditors of the Debtor and of the Subsidiary Debtor, the Commission, the Secretary of the Treasury of the United States and all other interested parties.

[fol. 233a] 10. The Plan has been duly submitted to all classes of security holders entitled to vote thereon and the form and method of such submission fully satisfy all requirements of law.

11. The Plan has been duly accepted by or on behalf of creditors and stockholders of each class to which submission is required under subsection (e) of Section 77 holding more than two-thirds in amount of the total of the allowed claims of each class, which have been reported in said submission and in said certificate of the Commission as voting on the Plan except the holders of the General Mortgage Bonds of the Debtor.

12. Such acceptances have not been made or procured by any means forbidden by law.

13. The Plan makes adequate provision for fair and equitable treatment for the interests or claims of the holders of the General Mortgage Bonds of the Debtor.

14. The rejection of the Plan by the holders of the General Mortgage Bonds of the Debtor is not reasonably justified in the light of their respective rights and interests and all the relevant facts.

15. The Plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of subsection (e) of Section 77, and, without limiting the generality of the foregoing language,

> (i) The plan complies with the provisions of subsection (b) of Section 77, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in

favor of any class of creditors or stockholders, and conforms and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders;

(ii) All amounts to be paid by the Debtor or the Subsidiary Debtor, or by any corporation or corpora-
[fol. 234] tions acquiring the assets of the Debtor or the Subsidiary Debtor, for expenses and fees incident to the reorganization, have been fully disclosed so far as they could be ascertained at the date of such hearing, namely, for the period through July 1, 1943; the Commission has fixed maximum limits in respect to the amounts to be allowed for such expenses and fees and by an order entered April 14, 1941 (Order No. 333, Rec. 7755) and by an order entered May 3, 1944 (Order No. 536); this Court made such allowances as it deemed reasonable within such maximum limits. Such additional amounts as may be required to be paid by the Debtor or the Subsidiary Debtor, or any corporation or corporations acquiring the assets of the Debtor or the Subsidiary Debtor for expenses and fees incident to the reorganization in respect of the period after July 1, 1943, can not be ascertained at this time, but, by virtue of the Plan and this Order, such amounts will be subject to maximum limits therefor to be hereafter fixed by the Commission and will within such maximum limits be subject to the approval of this Court; and

(iii) The Plan provides for the payment of all costs of administration and all other allowances made or to be made by this Court.

16. By various orders entered in this proceeding the Trustees, or the Debtor, while under the control of this Court, have been authorized to enter into various agreements, contracts, instruments and leases extending beyond the period of this reorganization proceeding. Said orders provide that as a condition to the conclusion of these proceedings or the turn-over of the estate the Debtor or any person or corporation acquiring the Debtor's property shall be or become bound by all the terms and provisions of such agreements, contracts, instruments and leases. [fol. 235] The Plan and this Order provide for the adoption

of all such agreements, contracts, instruments and leases by the New Company, and such conditions are accordingly satisfied.

17. The Plan duly satisfies all of the requirements of Section 77 for approval by the Commission and this Court and for confirmation by this Court and all steps necessary to be taken in connection therewith, and all things necessary to be done in connection therewith, by the Commission, this Court, the Debtor, its Trustees, the Subsidiary Debtor, its Trustee and all other persons, have been taken and performed in the manner and within the times required in Section 77 and in conformity with all requirements of Section 77 and all other applicable law.

18. The Plan should now be confirmed.

19. The Court has on November 1, 1944, filed in this proceeding an opinion containing a statement of its conclusions and reasons for confirming the Plan.

20. In conformity with Section Q of the Plan, Insurance Group Committee has duly designated Richard K. Paynter, Jr., and Eugene A. Schmidt, Jr., to be members of the Reorganization Committee provided for in the Plan; The Chase National Bank of the City of New York, as Trustee, and City Bank Farmers Trust Company, as Trustee, have duly designated J. F. Fitzpatrick to be a member of the Reorganization Committee; and Reconstruction Finance Corporation has duly designated Frank C. Wright to be a member of the Reorganization Committee. Under said Section Q this Court is empowered to designate a member of the Reorganization Committee and upon such designation the Reorganization Committee will be duly constituted and will have the powers and authority provided for in the Plan as the Reorganization Committee and as the Voting Trustees provided for in the Plan.

[fol. 236] 21. The term "parties in interest", wherever used herein, shall, without hereby limiting the generality thereof, include the Debtor, the Subsidiary Debtor, all creditors and stockholders of the Debtor or the Subsidiary Debtor, all indenture trustees, all parties to these proceedings and all other parties in interest.

22. The findings herein shall be taken and deemed to be findings of fact, and, in addition, to the extent appropriate, conclusions of law and also orders.

It Is, Therefore, Ordered, Adjudged And Decreed That

(a) The Plan be, and it hereby is, confirmed, and all objections thereto are severally overruled.

(b) The provisions of the Plan and of this Order shall forthwith become and be, and are hereby declared to be, final and binding, upon the Debtor and the Subsidiary Debtor, and all of their respective stockholders, including those who have not, as well as those who have, accepted the Plan, and all creditors of the Debtor or the Subsidiary Debtor, secured or unsecured, whether or not adversely affected by the Plan, and whether or not their claims have been filed, and, if filed, whether or not approved, including creditors who have not, as well as those who have, accepted the Plan, and upon any and all other parties in interest.

(c) No payments shall be made by the Debtor or the Subsidiary Debtor or any corporation or corporations acquiring the assets of the Debtor or the Subsidiary Debtor for services performed or expenses incurred (including reasonable attorney's fees) after July 1, 1943, in connection with the proceeding or the Plan, or in connection with the carrying out of the Plan, or incident to the reorganization, except as may be hereafter authorized by further order of this Court within maximum limits hereafter to be fixed by the Commission.

[fol. 237] (d) The rights of all stockholders and creditors of the Debtor and the Subsidiary Debtor and of all other parties in interest shall be only those provided by the Plan.

(e) The Debtor, the Subsidiary Debtor and any new corporation organized to receive the properties of the Debtor or the Subsidiary Debtor upon the consummation of the Plan be, and each of them hereby is, authorized and directed, and shall have full power and authority, to take all steps, and do all things, necessary on its or their part to put into effect and carry out the Plan and the orders of this Court relative thereto, under and subject to the supervision and control of this Court, the laws of any State or the decision or order of any State authority to the contrary notwithstanding.

(f) The Court hereby designates John Evans to be a member of the Reorganization Committee.

(g) The Reorganization Committee, pursuant to the provisions of Section 77 and the Plan, and with all the powers and immunities provided in Section 77 or the Plan, shall have full power and authority, subject to the supervision and control of this Court, to put into effect and carry out the Plan and the orders of this Court relative thereto; provided, however, that the Plan shall not be submitted to the holders of the Income Bonds of The Denver and Salt Lake Railway Company, and the Plan shall not be consummated, until the appeal taken from this Court's said Order of October 25, 1943, shall be dismissed or finally decided in such manner as to affirm such Order and until any appeal taken from this Order shall be dismissed or finally decided so as to affirm this Order, or until further order of this Court.

(h) As provided in said Section Q of the Plan the members of the Reorganization Committee, in their capacity as members of such committee and in their capacity as Voting [fol. 238] Trustees shall not be liable for any action taken by them in good faith or by any person employed by them in good faith, except for their respective individual malfeasance or willful neglect. The members of the Reorganization Committee, and their successors, if any, and each of them, be, and they are and he is hereby, relieved of all personal liability to any person, firm or corporation for acts done pursuant to prior approval of this Court. The Reorganization Committee shall report to the Court all action taken by them without prior approval of this Court, and, upon approval by this Court, such members and each of them shall be relieved from all personal liability to any person, firm or corporation therefor. To the extent necessary to give effect to the provisions of this paragraph, the members of the Reorganization Committee shall be indemnified and held harmless against any loss, liability or expense by the Trustees, the Debtor, the Subsidiary Debtor and any corporation receiving the properties of any of them upon the consummation of the Plan.

(i) This order shall become, and it is hereby declared to be, effective immediately upon its entry in this proceeding by the signature of the Judge of this Court.

(j) The Court reserves full jurisdiction to construe the Plan, to cure any defect, supply any omission and reconcile any inconsistency in the Plan and to exercise all its powers under the Plan, all in such manner and to such extent as may be necessary or expedient to carry out the Plan effectively.

(k) The Court retains full jurisdiction of this proceeding and of all parties in interest for the purpose of entering such other and further orders as may be appropriate.

Dated November 29th, 1944.

By the Court, (S.) *J.* Foster Symes, *Judge.*

[File endorsement omitted.]

[fol. 239] United States Circuit Court of Appeals,
Tenth Circuit, November Term, 1944

Nos. 2906, 2907, 3106, 3107 and 3108

In the Matter of The Denver and Rio Grande Western Railroad Company, a Corporation, Debtor

No. 2906

The Denver and Rio Grande Western Railroad Company, a Corporation, Debtor, Appellant,

vs.

Insurance Group Committee; Reconstruction Finance Corporation; Wilson McCarthy and *Henry Swan*, as Trustees of The Denver and Rio Grande Western Railroad Company, a Corporation; the Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; City Bank Farmers Trust Company, a Corporation, as Trustee; The United States Trust Company of New York, as Trustee; and Central Hanover Bank and Trust Company, as Trustee, Appellees

Appeals from the United States District Court for the District of Colorado

[fol. 240] No. 2907

The Denver & Salt Lake Western Railroad Company, a Corporation, Debtor, Appellant,

vs.

Insurance Group Committee; Reconstruction Finance Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a Corporation; The Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; City Bank Farmers Trust Company, a Corporation, as Trustee; The United States Trust Company of New York, as Trustee; and Central Hanover Bank and Trust Company, as Trustee, Appellees

Appeals from the United States District Court for the District of Colorado

No. 3106

CITY BANK FARMERS TRUST COMPANY, a Corporation, as Trustee under the General Mortgage, February 1, 1924, of The Denver and Rio Grande Western Railroad Company, Appellant,

vs.

INSURANCE GROUP COMMITTEE; RECONSTRUCTION FINANCE CORPORATION; Wilson McCarthy and Henry Swan, as Trustees of The Denver and Rio Grande Western Railroad Company, a Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a corporation; The Moffat Tunnel Improvement District; Moffat Tunnel Commission; Guy A. Thompson, as Trustee of the Missouri Pacific Railroad Company; The Denver and Rio Grande Western Railroad Company, [fol. 241] a Corporation, Debtor; The Denver & Salt Lake Western Railroad Company, a Corporation; Subsidiary Debtor; State of Colorado; Colorado Public Utilities Commission; The United States Trust Company of New York, as Trustee; The Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; Central Hanover Bank and Trust Company, as Trustee; Untermyer Family Group; General Securities Company; and Bankers Trust Company, as Trustee, Appellees

Appeals from the United States District Court for the District of Colorado

No. 3107

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, a Corporation, Debtor; and The Denver & Salt Lake Western Railroad Company, a Corporation, Subsidiary Debtor, Appellants,

vs.

INSURANCE GROUP COMMITTEE; CITY BANK FARMERS TRUST COMPANY, a Corporation, as Trustee; Reconstruction Finance Corporation; Wilson McCarthy and Henry Swan,

as Trustees of The Denver and Rio Grande Western Railroad Company, a Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a Corporation; The Moffat Tunnel Improvement District; Moffat Tunnel Commission; Guy A. Thompson, as Trustee of the Missouri Pacific Railroad Company; State of Colorado; Colorado Public Utilities Commission; The United States Trust Company of New York, as Trustee; The Chase National Bank of the City [fol. 242] of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; Central Hanover Bank and Trust Company, as Trustee; Untermyer Family Group; General Securities Company; and Bankers Trust Company, as Trustee, Appellees.

Appeals from the United States District Court for the District of Colorado

No. 3108

GUY A. THOMPSON, as Trustee of the Missouri Pacific Railroad Company, Appellant,

vs.

INSURANCE GROUP COMMITTEE; CITY BANK FARMERS TRUST COMPANY, a Corporation, as Trustee; Reconstruction Finance Corporation; Wilson McCarthy and Henry Swan, as Trustee of The Denver and Rio Grande Western Railroad Company, a Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a Corporation; The Moffat Tunnel Improvement District; Moffat Tunnel Commission; The Denver and Rio Grande Western Railroad Company, Debtor; The Denver & Salt Lake Western Railroad Company, Subsidiary Debtor; State of Colorado; Colorado Public Utilities Commission; The United States Trust Company of New York, as Trustee; The Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; Central Hanover Bank and Trust Company, as Trustee; Untermeyer Family Group; General Securities Company; and Bankers Trust Company, as Trustee, Appellees

[fol. 243] OPINION—[May 10, 1945]

Before Phillips, Huxman, and Murrah, Circuit Judges.

William V. Hodges (F. C. Nicodemus, Jr.; Hodges, Vidal and Goree; and Pierce and Greer were with him on the brief) for Denver & Rio Grande Western R. Co., and Denver, Salt Lake Western R. Co.

Edward E. Watts, Jr., and Milton J. Keegan (Peter H. Holme; Mitchell, Capron, Marsh, Angulo and Cooney; and Dines, Dines and Holme were with them on the brief) for appellant City Bank Farmers Trust Company.

H. H. Larimore (J. W. Preston and R. L. Dearmont were with him on the brief) for appellant Guy A. Thompson, Trustee.

George D. Gibson and Henry W. Anderson (Grant, Shafroth and Toll; Hunton, Williams, Anderson, Gay & Moore; and Nan Ross McConnell were with him on the brief) for appellees Insurance Group Committee.

Norma L. Comstock; Alexander M. Lewis; and Rathbone, Perry, Kelley and Drye on the brief for appellee Central Hanover Bank and Trust Company, Trustee.

Edwin S. S. Sunderland (Pershing, Bosworth, Dick and Dawson; Davis, Polk, Wardwell, Sunderland and Kiendl; Thomas O. G. Fitzgibbon; and Judson C. McLester, Jr., were with him on the brief) for appellee Guaranty Trust Company of New York, Trustee.

James L. Homire (James A. Marsh and Emmet McCaffery were with him on the brief) for appellee Reconstruction Finance Corporation.

Lindsey and Larwill; Daniel K. Wolfe; and Stewart and Shearer on the brief for appellee United States Trust Company of New York, Trustee.

Lewis and Grant; Milbank, Tweed and Hope; and Arthur A. Gammell on the brief for appellee The Chase National Bank of the City of New York, Trustee.

[fol. 244] HUXMAN, Circuit Judge, delivered the opinion of the court.

The Denver and Rio Grande Western Railroad Company[1] and the Salt Lake Western Railroad Company, the second debtor,[2] filed their petitions in the United States District Court for the District of Colorado November 1, 1935, for reorganization under Section 77 of the Bankruptcy Act of July 1, 1898, as amended, 11 USCA, § 205. The petitions were approved on the same day, trustees were appointed, and the Debtor was authorized and directed to maintain and operate its property under this proceeding. The Debtor has now been in court under this proceeding for nearly ten years. The Debtor had outstanding numerous senior securities[3] which were secured by liens on various parts of the property embraced in the railroad system. These were preferred claims, superior in rank to all other claims against the Debtor. There are no issues or contests between the holders of these classes of securities and it is not necessary to treat them separately. They will be referred to collectively as Senior Bondholders. In addition to these bonds, the Debtor had outstanding general mortgage bonds, in the amount of $29,808,000, which were subordinate in rank only to the claims of the Senior Bondholders. They will be referred to as General Bondholders. The Debtor also had outstanding preferred stock and common stock.

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[1] Herein called the Debtor.

[2] The property of the second debtor became a part of the system property under the plan of reorganization. No separate questions arise by virtue of this debtor, and reference to it will not be necessary in the course of the opinion.

[3] These securities were as follows (not including certain bonds pledged to R. F. C. or Chase Bank to secure their notes hereinafter mentioned):

$15,190,000 Rio Grande Western first mortgage 4's.
15,080,000 Western Consolidated 4's.
2,000,000 Rio Grande Junction First 5's.
34,125,000 Denver Rio Grande Consolidated 4's.
6,382,000 Denver & Rio Grande Consolidated 4½'s.
12,000,000 Refunding and Improvement 5's.
2,000,000 Refunding and Improvement 6's.
A note to the Chase National Bank for $1,500,000.
Notes to the R. F. C. in the total sum of $10,691,850.
And equipment obligations in the sum of $2,325,000.

The contest in this case arises between the holders of securities of different rank or priority, by virtue of the fact that the total capitalized value found by the Commission for [fol. 245] the reorganized company is insufficient to satisfy in full all claims against the Debtor. The plan of reorganization under consideration satisfied in full the claims of the Senior Bondholders, by assigning to them new securities and common stock for the full amount of their claims. There was left common stock of the Debtor sufficient only to pay ten per cent of the claims of the General Bondholders, and nothing for the holders of the preferred stock and of the common stock. Their claims were adjudged worthless and they were barred from participating in the assets of the reorganized company.

Ten different plans of reorganization were proposed and considered by the Commission prior to the plan which was finally adopted and which is in controversy herein. Two plans were submitted to become effective January 1, 1937. One placed a valuation on the property of $149,732,966, and the other a valuation of $158,747,766. Both gave the General Bondholders 100 per cent of the value of their claims in new stock. Thereafter seven other plans were proposed. They gave the General Bondholders from 32.99% to 50% of their claims in new stock. The valuation placed on the Debtor's property in these plans varied from $135,005,436 to $161,631,934. The Interstate Commerce Commission submitted a third plan, effective January 1, 1942, which gave the General Bondholders five per cent of their claims in new stock. It valued the property at $142,846,612. Thereafter the Interstate Commerce Commission submitted a fourth plan, which is the one under consideration here. This plan is in the alternative. One provides for consolidation with the Denver and Salt Lake Railroad Company. The alternative does not provide for such consolidation. In the event of consolidation, the capitalized valuation placed on the property was $155,173,127. If there was no consolidation, then the capitalized valuation was fixed at $143,528,027. As stated, this plan gave the General Bondholders only ten per cent of the value of their claim in common stock, and barred the preferred stockholders and the common stockholders from participation in the reorganized company. For the purpose of the questions presented by this appeal, it is immaterial which valuation is considered.

On May 1, 1943, after the final plan, as outlined above, had been approved by the Commission, the Debtor filed a petition [fol. 246] with the Commission requesting that the proceedings be reopened for the introduction of additional evidence pertaining to the then existing economic conditions and the prospective earnings of the new company as they might affect the capitalization of the new company, the value of the property, and other elements of the plan. The Commission found that such additional evidence was not required and denied the petition. Thereafter the proposed plan was submitted to the District Court for its consideration.

On September 16, 1943, while the court had the plan under consideration, it entered an order providing that the Junction Bonds,[4] for which provision had been made in the capital structure, be paid from surplus cash in the hands of the Debtor's trustees. On October 25, 1943, the court entered an order approving the plan. Thereafter, on March 31, 1944, the trustees of the General Bonds filed an application with the District Court for a redistribution of the securities which had been set apart in the capital structure for the Junction Bonds. On April 26, 1944, the Commission submitted the plan to the creditors for acceptance or rejection. The General Bondholders rejected the plan by a vote of 20.67% for to 79.33% against the plan. The result of this vote was certified to the District Court. On November 29, 1944, the District Court entered a final order overruling the objections to the confirmation of the plan and denying the application for a redistribution of the securities set up for the Junction Bonds, and confirmed the plan. Appeals have been prosecuted both from the order of October 25, 1943, approving the plan, and from the final order of November 29, 1944. Both appeals present the same questions and they will not be separately treated. The questions urged by the various appellants will be considered without reference to the appellant presenting them.

Numerous assignments of error are urged by the various parties. They may be summarized generally as follows:

1. The Commission employed fundamentally erroneous methods of valuation in valuing the property of the new company.

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[4] The facts concerning these bonds will be developed later.

[fol. 247] 2. The Commissioner erred in denying the petition of the Debtor asking that the case be reopened for the consideration of additional evidence pertaining to the then existing economic conditions and the prospective earnings of the new company as they might affect the capitalization of the new company.

3. The plan is not fair and equitable and fails to afford due recognition to the rights of all classes of creditors and discriminates unfairly in favor of the Senior Mortgage Bondholders, within the meaning of Sec. 77(e) of the Act.

4. The rejection of the plan by 77% of the General Mortgage Bondholders, voting at an election for that purpose, deprived the court of the power to approve and confirm the plan.

5. The court erred in refusing to redistribute the securities intended for the Junction Bonds when they were paid from cash, so as to give the benefit thereof to the General Bondholders.

Method of Valuation

The Act provides that in valuing the property, the Commission shall give due consideration to earning power, past, present, and prospective, as well as all other relevant facts.[5] While the Commission's report recites that it gave consideration to all relevant factors, it must be conceded that the valuation was fixed almost entirely on the basis of earning power of the property.

Reproduction cost new less depreciation, and invested capital were stressed in the oral argument as fundamentally correct methods of valuation which must be considered as factors and taken into account in any proper valuation of a utility property. It is urged that the valuation of the Commission is fundamentally erroneous because these factors were disregarded.

A railroad is a utility, impressed with a public interest. The very existence of our nation depends upon a sound, efficient, transcontinental transportation system. The purpose of Section 77 is to provide an efficient and speedy

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[5] 11 USCA § 205(e).

[fol. 248] method of reviving sick and ailing railroads. It recognizes the rights of creditors and stockholders of the road. It preserves their interests in the property and maintains the rank and priorities of various classes of creditors. In addition to all this, it seeks to reorganize the road, to place it on a sound financial footing, so that it may continue to operate and serve the nation's needs.

The effective administration of Section 77 requires a reexamination and revaluation of the property of the railroad system. The primary question for the Commission is what value can be established upon which the road may expect to earn a reasonable return. Prospective earnings is a proper method by which to determine the new valuation of a railroad. In fact, it is the only method which can insure the continued operation of a railroad without recurring receiverships. The use of any method that does not reflect earning power is but a stop-gap on the road to bankruptcy. To provide that the new capitalization should not be less than the cost of reproduction new less depreciation, or not less than the capital investment would in itself be of no benefit to junior creditors if such value bore no sound economic relation to prospective earnings, because the earnings would be insufficient to pay their claims, and in the end their new securities would be as valueless as their present ones now are.

In Ecker v. Western Pac. R. Co., 318 U. S. 448, and Group of Investors v. Milwaukee R. Co., 318 U. S. 523, the Supreme Court definitely placed its stamp of approval upon prospective net earnings as a proper method of valuing a railroad in a reorganization proceeding under Section 77. In the Milwaukee case, the Supreme Court said:

> "The basic question in a valuation for reorganization purposes is how much the enterprise in all probability can earn."

The court points out that a disregard of that method of valuation can bring only a harvest of barren regrets. The court also points out in the Milwaukee case that the Commission may disregard other methods of valuation if in its opinion they afford no reasonable basis for believing that the probable earning power of the road is greater than [fol. 249] what the Commission had found by considering the prospective earnings. This all sums up to the conclu-

sion that earning power is the factor around which a reorganization must be built. We find no error in the use by the Commission of prospective earnings as the method of valuing the property of the Debtor.

It is urged that in any event the action of the Commission was arbitrary because it considered earnings only during the depression years and gave no regard to present or prospective earnings. This is not borne out by the record. The Commission reviewed and considered the earning history of the Debtor for the past 24 years. This included normal years and depression years, as well as abnormal war years. From all of this the Commission estimated the probable prospective earnings and based its valuation thereon. It is true that it did not give much consideration to the present inflated war earnings. For this it cannot be criticized. These earnings are to a great extent artificial, and will disappear largely with the coming of the peace. They have very little value in estimating the probable future earnings of this property in the peace economy which is to come. The Commission was well within its right in largely disregarding them in reaching its conclusions as to the probable prospective earnings of the property. See Group of Investors v. Milwaukee R. Co., supra, page 544.

It is further urged that the Commission fell into reversible error in failing to take into account new war industries which have been erected at various points on the system. Such industries have been erected and are operating as a part of our war economy. Who can now say how many of those, if any, will remain after the war and will continue to contribute to the income of the Debtor? Such factors are in the outer realm of speculation. No one can say with any degree of certainty what their future place in the economic world will be. Neither can it be said with any degree of sureness how much, if any, net revenues these industries will contribute to the system. In this situation it cannot be said the Commission erred in refusing to give such factors a prominent place in the capitalized value of the system based on prospective earnings. It did consider all of these factors, and from a view of the entire field, reached its conclusion as to the probable prospective earning capacity of the system.

[fol. 250] It is urged that the plan is fatally defective because the Commission refused to capitalize the excess

surplus current assets and thus make available more new securities for the General Bondholders. As of December 31, 1935, the Debtor had a deficit in its net working capital account of $9,727,230. December 31, 1942, the effective date of the plan, its net working capital was $6,811,077. December 31, 1943, the net working capital had increased to $10,398,084, and by December 31, 1944, the surplus had risen to $12,125,863.50. From this it will be observed that there was on hand an unusually large amount of current assets. We have already held that the Commission was on sound ground in giving little consideration to war profits in considering future prospective earnings. By the same reasoning, it was well within its rights in refusing to capitalize them and set them up as a part of the permanent capital structure of the company.

It is urged that the valuation of the Commission is fatally defective because it does not reflect extensive and valuable additions and betterments which were made by the trustees in this proceeding. At least since 1939 the Debtor has enjoyed substantial net income. The trustee's annual reports show that since the institution of this proceeding, the Debtor's net earned income has exceeded $50,000,000, and that more than $43,000,000 of this has been used in making permanent betterments and improvements. Many of such improvements substantially increased the potential earning capacity of the railroad. To illustrate: central train control was installed in many segments of the road where the greatest density of traffic obtained, thereby giving to such sections of the road the equivalent of a double track road. All of this has resulted in greatly increasing the efficiency and economy in the handling of traffic. It is true that as a result of these vast expenditures of the net earnings, the railroad has been greatly improved and the present owners will be handed a substantially new railroad system.

It is also true that the valuation adopted by the Commission does not reflect these improvements in the sense that the valuation was substantially increased over the value which had been placed on the property prior to the [fol. 251] time these improvements were made. But this in itself does not condemn the action of the Commission. The question for its determination was the earning capacity of this property. These improvements were considered by the Commission, and no doubt taken into ac-

count, together with all the other facilities of the road, in reaching its conclusion as to what the property reasonably could be expected to earn. It is not unreasonable to assume that if these improvements had not been made, the probable earning capacity would have been substantially reduced. This in turn would have resulted in a reduced valuation, which in turn would have reduced the participation of the General Bondholders in the reorganized company. It cannot be said, therefore, as a matter of law, that the General Bondholders will not receive some benefit from these expenditures. Whether these funds were wisely or equitably used for the benefit of all classes of creditors is not an issue in the present posture of the case. The question still is, does the valuation of the Commission bear reasonable relation to the prospective earning capacity of the road; and is the action of Commission in setting up the capital structure free from legal infirmities which require us to reject the plan?

It is also urged that the Commission erred in refusing to reopen the proceedings for the introduction of additional evidence pertaining to the then existing economic conditions and to the prospective earnings of the Debtor as reflected by the 1943 income. The record reveals that there was a substantial increase in the earnings of 1943 over 1942, but it is also shown that the increased cost of operation more than offset this increase and that the net income for 1943 was less than for 1942. This further evidences the difficulty in basing a valuation upon distorted conditions resulting from an all-out effort in a global war. This case has been before the Commission and before the court for nearly ten years. During all this time, all factors have been continuously considered, valuations have been made and rejected, and other valuations have been made. There must come a time when the matters should be determined and the proceedings closed. There was no reversible error in the refusal of the Commission to reopen the proceedings for further consideration of these matters.

It is settled beyond the question of a doubt by the deci- [fol. 252] sions of the Supreme Court in Ecker v. Western Pac. R. Co., and Group of Investors v. Milwaukee R. Co., supra, and in the special concurring opinions of Justice Roberts in those cases, that the duty of formulating a plan of reorganization under Section 77, including the adoption

of a new valuation of the property, is a function confided to the Interstate Commerce Commission, and that no court of law may interfere with such plan or valuation because it does not agree with it. The members of the Interstate Commerce Commission are skilled and well versed by long experience in the handling and determination of such problems, and Congress wisely charged them with the primary responsibility of administering the reorganization of railroads under Section 77. Courts may interfere with the capital structure or valuation made by the Commission in a proceeding under this Act only when it can be said as a matter of law that the Commission used fundamentally erroneous methods of valuation or acted arbitrarily or capriciously. An examination of the entire record leads to the conclusion that the action and the conduct of the Commission in fixing the valuation and setting up the capital structure is free from these infirmities, and that its action in relation thereto must be upheld.

As pointed out, Congress in passing Section 77 intended to place the reorganization of railroads largely under the jurisdiction of the Interstate Commerce Commission, with limited power of review in the federal courts. Aside from the limited power of review of the valuation by the Commission and of the plan of reorganization to see that they conform to constitutional requirements, the primary function to be performed by the courts is provided for in Section 77(e). Under this section it is the duty of the District Court to examine the plan to see whether it complies with Subsection (b), and whether it is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the various classes of creditors and stockholders. If the court is satisfied that these requirements have been met, it must approve the plan, otherwise it should disapprove and return it to the Commission for further consideration.

[fol. 253] As already pointed out, the District Court performed this function. It considered the plan, approved it in its order of October 25, 1943, and confirmed it in its order of November 29, 1944. On appeal, our scope of review is more limited than even that of the District Court. We inquire only to ascertain whether the District Court per-

formed its judicial functions under Subsection (c) and whether its conclusions find support in the record. We may not reverse the District Court merely because we would have reached a different conclusion. As stated by the Supreme Court, "If there is warrant for the action of the District Court, our task on review is at an end." Group of Investors v. Milwaukee, supra.

It is urged that there is no warrant in the record for the District Court's finding that the plan is fair and equitable and affords due recognition to the rights of all classes of creditors. The District Court found that the findings of fact by the Commission were supported by evidence and the findings of the Commission were accordingly adopted by reference as the findings of fact of the court.

In considering whether the plan is fair and equitable, affords due consideration to the rights of each class of creditors, and whether it does not discriminate unfairly in favor of one class at the expense of another, our problem is to determine whether within the framework of the capital structure set up by the Commission the assets have been distributed to the various classes of claimants within the rule of Northern Pac. Ry. v. Boyd, 228 U. S. 482, and Consolidated Products Co. v. DuBois, 312 U. S. 510. These cases merely reiterate the well established equitable rule that property of an insolvent corporation must be used to satisfy in full the claims of various classes of creditors according to their priority in rank.

It is not claimed that of the securities issued under the capitalization authorized by the Commission, more has been set over to the Senior Bondholders than is required to satisfy their claims in full, with the exception of the items hereinafter noted. But the argument is made that the capitalization should be increased by virtue of the permanent improvements made from net earnings during the receivership and by virtue of the large amount of current assets so as to afford more securities or common stock for [fol. 254] the General Bondholders. We have already disposed of the contention that the earnings which were invested in permanent improvements and betterments should be reflected in increased capitalized value, and nothing further needs to be said on this point.

The mere fact, however, that cash and current assets are not required to be reflected in the capital structure in the

form of capitalized value does not remove them from the picture. They are nevertheless, assets of the corporation which must be taken into account in drawing up a fair and equitable plan of reorganization, and must be distributed in a manner that is fair and equitable to all classes of creditors. The Senior Bondholders were paid in full. They received all the new securities and most of the common stock. Ninety per cent of the General Bondholders' claims were wiped out. They received only a small amount of common stock, ten per cent of their total claim.[6] Adequate operating funds are essential to the operation of a railroad. The Senior Bondholders were entitled to receive in addition to the full amount of their claims, working capital sufficient for proper and efficient operation of the railroad. But anything in excess of what was reasonably necessary for this purpose constituted assets of the insolvent corporation which belonged to the remaining creditors.

We think it is apparent from the record that there were current assets on hand consisting of cash and securities in excess of what was needed for the efficient operation of the road. As pointed out, the working capital of the debtor had increased from a deficit of $9,727,230 as of December 31, 1935, to a surplus of $12,125,863.50 as of December 31, 1944. While these increased net earnings are due in large part to the war and will not continue after the end of the war, and may therefore be disregarded in setting up the capitalized structure based upon prospective earnings, we cannot disregard the fact that these huge surpluses actually exist. Their existence is an accomplished fact. It is also obvious that surpluses will continue to pile up for a reasonable time yet to come. We think any plan which fails to take this into account and which gives the Senior Bond- [fol. 255] holders their claims in full by substantially delivering the road to them, and gives them the surplus cash actually on hand and further enables them to receive in addition the excess war profits which are reasonably sure to come, is inherently inequitable and unfair, so long as there are classes of creditors whose claims are not fully satisfied.

The appellees urge that we must view the picture as of

[6] For the purpose of developing this point, the Senior Bondholders will be treated as the new owners of the railway system.

June 14, 1943, and that at such time there were no surplus current assets on hand. The conclusion is inescapable that on either June 14, 1943, or December 31, 1943, there were on hand surpluses greatly in excess of what was necessary for the proper operation of the railroad. The Commission was cognizant of the fact that surpluses were accumulating from war profits. Throughout its deliberations, it discussed excess war earnings. The trial judge, who was operating the road under the bankruptcy proceedings, and who had intimate knowledge of the financial status of the Debtor, recognized that excessive current assets had accumulated. In his order of September 13, 1943, directing the payment of the Junction Bonds in cash, the court said: "The trustees having on hand an amount of cash *far in excess* of the needs of reorganization expenses, including working capital . . . ."

The inherent weakness in the plan was not only that it did not make equitable distribution of the excess current assets on hand, but also that it failed to provide for the equitable distribution of excess war profits which could reasonably be expected to accrue during the rest of the war period. This is especially significant in view of the complaint by the General Bondholders of the use which was made of the net earned profits during the period of the trusteeship.

They complain that practically all the net profits were used in making over the road instead of paying debts and that as a result debts mounted to a point where their equity in the property decreased from a 100 per cent participation in the capitalized structure under the first plan to a mere 10 per cent under the final plan. That they have a real grievance is apparent from the record.

On November 1, 1935, the Debtor's total debts senior to the claim of the General Bondholders was slightly over [fol. 256] $101,000,000. The General Bondholders' claims at that time were approximately $30,000,000, making the total of the two claims approximately $131,000,000. Any one of the ten plans of reorganization prior to the final one fixed the value of the property at more than enough to satisfy the claims of all bondholders in full, as of the date this proceeding was instituted. During the ten intervening years, the claim of the Senior Bondholders increased to more than $139,000,000, and that of the General Bond-

holders to more than $43,500,000, making a total of more than $482,000,000, required for the two classes of claims.

During all of this period the Debtor enjoyed substantial income, amounting to approximately $50,000,000. Instead of using this income in payment of interest on the senior claims, it was used in making permanent and lasting improvements in the road. More than $43,000,000 was used in this way. None of these expenditures has resulted in a comparable increase or in any substantial increase in the final valuation, over the valuation prior to the making of the improvements. But as a result of this operation, the position of the General Bondholders has deteriorated from a 100 per cent participation of the amount of their claims to a mere ten per cent. Nor does it change the picture to say that these improvements were necessary to the railroad system. The fact still remains that earnings in which all had a vital interest were used in building a new railroad in many respects, which will be handed over to the Senior Bondholders, and the General Bondholders will practically be eliminated as a result thereof.

But this alone does not entitle the General Bondholders to a greater participation in the reorganized company. Neither does it condemn the plan of reorganization or the capital structure set up therein. The operation of a railroad involves the expenditure of large sums for operation. It involves the formulation of plans of operation and the exercise of judgment and discretion. If, in the exercise of this discretion, funds are unwisely spent, from the viewpoint of the interest of all creditors, they may feel aggrieved, but they have no legal cause of complaint.

Neither was the Commission compelled to, nor would it [fol. 257] be justified in adding the amount of these expenditures to the capitalized value if in the exercise of sound discretion it felt that the reasonable prospective earnings of the road after the improvements did not justify it. However, in the face of all this, after satisfying in full the claims of the senior bondholders, the plan of reorganization should have made sure that all excess current assets, as well as all excess war profits yet to accrue, would go to the General Bondholders.

The commission, as pointed out, adopted a conservative, sound estimate of the prospective earnings of the reorganized company. For this it is not to be criticized. An over-

optimistic view would again surely lead the Debtor into the bankruptcy courts, with which it has had too much acquaintance already.[7] We, however, feel that there is more than a speculative probability that these war industries which have been constructed along the system, as well as the improvements which have been made by the use of these net earnings, might produce greater net returns than anticipated in the plan. If such should be the case, they certainly belong to the General Bondholders and not to the Seniors, and the plan should bring this about. It could be done by issuing to the General Bondholders an additional amount of a subordinate stock which would receive returns only from excess dividends. This is a mere suggestion on our part, and in no wise binding on the Commission. Our duty is limited to pointing out defects in the plan. It is the responsibility of the Commission to correct them.

The Junction Bonds

We think that the complaint as to the manner in which the Junction Bonds were handled is well taken. The Rio Grande Junction Railroad is a wholly owned subsidiary of the Debtor. It had bonds outstanding in the hands of the public for the payment of which the Debtor was liable, totaling $2,758,333. This claim was senior to that of the [fol. 258] General Bondholders. The plan set aside securities for the payment of this claim. In an order dated September 13, 1943, the District Court directed the trustee to pay this claim with some of the surplus cash on hand, and retained the securities which were to be used in the payment thereof in the treasury of the company. The court treated the transaction as a purchase of securities rather than a payment of a debt. This is a play upon words, and, in any event, is immaterial to the issue. The fact remains that the new capitalization provided securities for the pay-

[7] Properties included in this railroad system have participated in the following reorganizations: The Denver & Rio Grande R. Co. was a successor in a reorganization proceeding in 1886; the Rio Grande & Western R. Co. was the successor in a reorganization proceeding in 1889; these two companies consolidated in 1908 under the name of the Denver & Rio Grande R. Co.; the present company was reorganized in 1920 and again in 1922 to 1924.

ment of these bonds. The value behind these securities in no wise belonged to the Senior Bondholders, because they had been paid in full. When surplus cash was used to pay this claim, the value behind the securities set aside for that purpose remained undistributed. Since the Senior Bondholders had been satisfied in full, this undistributed value in all equity and fairness belonged to the General Bondholders. Any plan which does not give it to them does not comply with the requirements of Section 77(e) of the Act.

Decrease in Senior Debt

Debts due to the senior creditors, which are all classified in this opinion as Senior Bondholders, included equipment obligations of $5,758,000. Under the plan, these claims are to be paid with new securities and are thus satisfied before the General Bondholders receive anything. As of December 31, 1944, the equipment obligations had been reduced to $4,540,000.[8] This resulted in a decrease in these obligations of $1,218,000. The new securities set apart for the payment of this sum will not be needed. If no further disposition is made of the securities provided for this debt, the value behind them will inure to the further benefit of the Senior Bondholders. What we have said with regard to the Junction Bonds applies with equal force here. It would be inequitable to give this additional value to the Senior Bondholders when they have already been fully compensated. This unused value belongs to the General Bondholders. This question has arisen since the adoption of the plan, and therefore cannot condemn the plan as it was [fol. 259] formulated and adopted, but since the proceedings must go back to the Commission, failure to take this change in Senior Bond requirements into account and make the capitalized value represented by these securities available to the General Bondholders would violate the requirements of Section 77(e).

Utah Fuel Company Stock

Complaint is also made of the manner in which the plan disposes of the capital stock of the Utah Fuel Company. The capital stock of this company consisted of 100,000

[8] See page 6, Income Account and Financial Exhibit, period ending December 31, 1944.

shares. All of it was pledged as collateral security for the payment of the first consolidated mortgage bonds of the Rio Grande Western Railway Company.[9] The Commission's amended order disposes of this collateral in the following manner; "* * * the trustee under the mortgage securing the R. G. Western Consolidateds [shall] be permitted to obtain the release of the equities * * * in the stock of the Utah Fuel Company, and distribute the stock among the holders of bonds in any manner acceptable to them, or to enforce its rights as pledgee of the stock, * * * [of the Utah Fuel Company] the proceeds recovered to be distributed to the holders of the bonds."

It is contended that the holders of the Rio Grande Western First Consolidated Mortgage Bonds should be compelled to either foreclose this collateral and apply the proceeds on their claim or should credit their claim with the value of this collateral and should then be allowed new securities for only the balance of their claim. It is contended that under the manner in which this collateral was treated, this class of claimants received more than full payment of their claim, at the expense of the General Bondholders.

There can be no question as to the duty resting upon these claimants to credit the value of this collateral upon their claim before sharing in the securities of the reorganized company. They were entitled only to full payment. If the new securities which were assigned to them satisfied their [fol. 260] claim in full, then the plan which permitted them to retain in addition this collateral would be inequitable and unfair to junior creditors.

The findings of the Commission are not clear as to the manner in which it treated this collateral. In its second supplemental report, of July 13, 1942, it states: "In our opinion, these bondholders are entitled to receive the beneficial interest in the Utah Fuel Company Stock in addition to the reorganization securities allotted to them." This language could be construed to mean that the Commission was of the opinion that it took this collateral, plus the new securities, to fully satisfy the claim of these creditors.

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[9] These obligations are a part of the claims referred to as the Senior Bondholders.

Neither does the record establish with any degree of satisfaction the value of this collateral. There is evidence which would support a conclusion that it had but little value. On the other hand, there is evidence that the Utah Fuel Company is now prosperous and is enjoying large earnings, with reasonable prospects that they will continue.

It appears to us that the plan contemplates that the claim of these creditors was to be satisfied from the new securities which were set apart for them, and that no particular value was ascribed to this collateral. If this collateral has any substantial value, it must be taken into account before the amount of new securities which are to be set over to these claimants is determined. The Commission should clear up the doubts and uncertainties which surround this matter when the proceedings are returned to it for further consideration.

It follows from what has been said that the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, and that the District Court was without authority to confirm the plan in the face of their adverse vote.

Under the admitted facts of the case, whether the plan complies with the requirement of Section 77(e) presents a pure question of law, and we are in no wise bound by the legal conclusions of the District Court in this respect. It is our conclusion that the plan fails to meet the requirements of Section 77(e) in that it fails to make equitable distribu-[fol. 264] tion of the surplus cash and current assets on hand; fails to make equitable provisions for the distribution of the excess war profits which may reasonably be expected to accrue; fails to make equitable and fair distribution of that part of the capitalized value represented by the securities set aside for the Junction Bonds. It is suggested that the District Court has power to make an equitable redistribution of the value represented by the undistributed securities, and that it is not necessary to remand this issue to the Commission. In view of the other questions which must be considered by the Commission, we deem it unnecessary to pass upon this question. We think the interests of all parties can best be served by having the entire matter reconsidered by the Commission and have it make all necessary adjustments.

Not much has been said about the claims of the preferred stockholders and the owners of common stock. It is quite apparent that no valuation based upon any reasonable estimate of prospective earnings could be sufficiently large to pay them anything. The finding that their claims are valueless and the order barring them from participation in the plan of reorganization is approved.

For the reasons herein stated, the order of the District Court of October 25, 1943, approving the plan, and its order of November 29, 1944, confirming the plan, are hereby reversed and the cause is remanded with directions to enter an order disapproving the plan, and remanding the case back to the Interstate Commerce Commission for its further consideration.

> "Nothing in this opinion shall prejudice or foreclose the rights of the parties to propose a new plan of reorganization or the power of the Commission to formulate, approve, and certify a new plan of reorganization in the light of any relevant facts presented to the Commission in any proceeding under 11 U. S. C. Sec. 205(d)."

It Is So Ordered.

[fol. 262] PHILLIPS, Circuit Judge, concurring:

The broad language of the Supreme Court in the Western Pacific case and the Milwaukee case[1] compels me to conclude that we cannot disturb the Commission's finding of valuation nor the finding of the Commission, confirmed by the trial court, that the equities of the unsecured creditors and the preferred and common stockholders have no value. Nevertheless, I feel impelled respectfully to suggest that the elimination of a substantial portion of the claim of the holders of the general mortgage bonds and all of the claims of stockholders and unsecured creditors, on the basis of a valuation resting wholly on an estimate of future earnings, is harsh treatment of such claims. I say this because, while according expertness to the Commission, it is my opinion that such future earnings cannot be estimated with

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[1] Ecker v. Western Pacific R. Corp., 318 U. S. 448;
Group of Investors v. Milwaukee R. Co., 318 U. S. 523.

a degree of certainty that is not likely to result in grave injustice.

The injustice to junior security holders which may result from a valuation based solely on an estimate of future earnings has aroused the attention of Congress and corrective legislation has been introduced. H. R. 4960 has already passed the House and is pending before a Senate Committee.[2]

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[2] The House Judiciary Committee, in its unanimous report (78th Cong., 2d Sess., Report No. 1615) recommending passage of H. R. 4960, in part said:

> "The purpose of the bill is to correct a very serious situation arising from the interpretation placed by the Interstate Commerce Commission and the courts upon the amendments of section 77 enacted by the Congress August 27, 1935. We believe this situation results from a misapprehension of the intention of Congress with respect to the 1935 amendments. The consequences have been and are so disastrous to railroad investors, and so dangerous to the credit of the railroads in general, that they should be corrected by legislation.
>
> "From a legal standpoint, the problem may be stated simply. Section 77 was directed primarily to the relief of financially embarrassed railroad companies through a revision of their capital structures and a reduction of fixed charges. It does not expressly provide for any reduction in the existing total capitalization; but the Interstate Commerce Commission has interpreted paragraph (d) of the section as authorizing it to fix the total capitalization of the reorganized company. In so doing, it has estimated a 'capitalizable value of the assets' of the property based almost entirely upon 'earning power'—earning power of the property, past, present and prospective—as these words are used in section 77(e). Its estimates of prospective earning power are necessarily speculative. Nevertheless it has used its estimates of earning power to fix capitalizations in all cases very substantially below the existing capitalizations, regardless of the investment in the property and of the valuation previously determined by the Commission under section 19a of the Interstate Commerce Act. The Supreme Court in

[fol. 263] On November 1, 1935, during the depths of the national depression, the debtor came into court for reorganization. At that time the debtor's senior debts ahead of the general mortgage bonds aggregated slightly over $101,000,000 and the claim of the general mortgage bondholders aggregated about $30,000,000. With an immediate reorganization, a capitalization of $132,000,000 would have been [fol. 264] adequate to give the general mortgage bondholders new stock equal to 100 per cent of their claim. No capitalization or valuation ever proposed for the debtor, in any plan presented, has been that low. During the eight years' delay in reorganization (in nowise due to the general mortgage bondholders, but, at least in part, to controversies among the senior security holders) and up to January 1, 1943, the effective date of the plan, the claims of the senior security holders, due to the accrual and nonpay-

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passing upon two major reorganization plans—the Western Pacific and the Chicago, Milwaukee, St. Paul & Pacific—upheld the Commission in this interpretation of the section, and has further held that the Commission's findings will not be disturbed where there is some evidence to support them. In other words, these administrative findings are beyond judicial review.

"The result of this interpretation of the statute by the Commission, and the subsequent refusal of the courts to review the Commission's findings, has caused the destruction of hundreds of millions of dollars of railroad securities representing actual investment in the property made, to some extent at least, in reliance upon the belief that such investments could not be confiscated except by due process of law.

. . . . . .

"In five major companies now undergoing reorganization, the reductions in capitalization aggregate some $600,000,000, meaning that this amount of railroad securities has been eliminated in the reorganization of these five companies alone, although there is no question that the investment in road and equipment and the 19a valuations at the present time are far in excess of the capitalization determined by the Commission. The

ment of interest, increased about $38,000,000. The debtor's net income available for interest during the trusteeship to the end of 1944 amounted to $19,420,972. It exceeded by approximately $9,500,000 the interest charges which accrued on the claims of senior security holders to the end of that [fol. 265] year. As of December 31, 1935, the debtor's current assets were $9,727,239 less than its current liabilities. As of December 31, 1944, the debtor's current assets exceeded its current liabilities by $12,125,863.50. Thus it will be seen there has been a favorable change in the current situation of $21,853,093, and, moreover, since the plan was formulated, the Junction Bonds have been paid and equipment obligations have been reduced from $5,758,000, the amount provided for in the plan, to $4,540,000, a reduction in that requirement of $1,218,000.

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same is true generally of the other roads involved in reorganization, these five being specifically mentioned, because they are included in one exhibit submitted to this committee by the Interstate Commerce Commission (hearings on H. R. 2857, serial No. 9, p. 199).

"That this situation has created an unbearable hardship upon the junior investors in railroad securities and constitutes a real danger to railroad credit may be easily seen from a glance at current railroad earnings. In 1942 the Missouri Pacific earned $32.67 a share on the common stock outstanding under the old capitalization; the Denver & Rio Grande Western, $34.40 a share; Rock Island, $25.11; Frisco, $18.03; St. Louis Southwestern, $27.23. These figures approximately were repeated in 1943; and the high earnings are continuing in 1944. Yet these stocks, which have demonstrated such an earning power, have been absolutely wiped out in reorganization, and the stockholders are without remedy. Moreover, the junior securities of all these roads have been drastically cut in reorganization and the senior securities have been very largely converted into income bonds and preferred and common stock. In one case, the Commission estimated a normal earning power of $11,000,000, and based its capitalization upon that figure; yet in the same year in which the Commission's plan was announced (1941) that road earned more than $18,000,000. In 1942, it earned $36,000,000,

Approximately $43,000,000 of the income available, but not used, for the payment of interest has been expended in permanent improvements and betterments. While the investment value of the debtor's property thus was substantially increased, the Commission's valuation, based on estimated future earnings, was not increased proportionately. As a result, the claim of the senior security holders has increased, and the participation of the general mortgage bondholders has been pressed downward until it is now fixed at 10 per cent of the new common stock. Many of the improvements and betterments referred to above, have substantially increased the capacity of the railroad to handle increased traffic as it arises. Central train control installed in many segments, where the greatest density of traffic obtains, gives to those segments, in a large degree, the equivalent of a double-track railroad and increases the

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and in 1942 $37,000,000. Nevertheless the Commission still says the old common stock is worthless. The stockholders are without remedy. There is in practical effect no judicial review of the action of the Commission. Although its guesses as to future earning power has been demonstrated to be wrong, its findings are final.

* * * * * * * * *

"The primary purpose of the bill is to insure that the courts shall make an independent judicial review of each plan and of the evidence upon which the plan is based. Under the existing statute, the Commission is required to certify to the court a transcript of its proceedings; and the court is required to notify all parties and, if objections are filed, to have a hearing. The effect of the proposed amendments is to require the judge to make an independent judicial determination of the facts found by the Commission, and not to hold that the administrative finding of the Commission is beyond judicial review. With this object in mind, the bill provides that the judge shall not only be satisfied that the plan complies with the provisions of subsection (b) as in the present statute, but must also be satisfied that it complies with the provisions of subsection (d), which the Supreme Court held was not within the province of judicial review. This will add nothing to the require-

number of trains that can be operated over the road and the volume of traffic that can be handled by the road. Other of such improvements have contributed to efficiency and economy in operations. These improvements have enabled the debtor to handle the great increase in traffic resulting from war effort and have placed the debtor in a position to more economically and efficiently handle a volume of traffic largely in excess of its prewar traffic, should future economic conditions produce such traffic. Under the plan approved and confirmed by the district court, 90 per cent of the common stock goes to the holders of the senior securities and 10 per cent to the general mortgage bondholders. As a result, should there be a substantial increase in the debtor's postwar traffic over its pre-war traffic, 90 per cent of the increased earnings will inure to the benefit of the holders of the senior securities and only 10 per cent [fol. 266] to the general mortgage bondholders, whose claim was decreased 90 per cent by reason of the failure to discharge interest accruals with income available therefor and the diversion of such income to the cost of such

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ments of the present statute as to the hearing and the scope of the evidence; it will merely direct the courts to exercise the traditional right of review, and to give the parties and the public the benefit thereof.

"Second, and as a means of insuring that the Interstate Commerce Commission shall be guided by some standard in determining the permissible capitalization of the reorganized company, the bill provides that the existing total capitalization shall not be reduced below the lower of either the investment in the property or the physical valuation as previously determined by the Commission under section 19a. Naturally, if the existing capitalization exceeds the investment, it should be susceptible of reduction, if the Commission finds it is not supported by earning power; or, if the existing capitalization exceeds the physical valuation found by the Commission, it should be susceptible of reduction, unless in that event the Commission deems the earning power sufficient to support it. But where the existing capitalization represents actual investment in the property, or where it is not in excess of the value determined by the Commission under the mandate of law, then it should not be disturbed."

permanent improvements. It seems to me, under all these circumstances, that, in addition to the other adjustments required to make the plan fair and equitable, the Commission should endeavor to modify the plan so as to give relief from the situation that lets the full impact of the improvement program fall upon the claim of the general mortgage bondholders and accords them no corresponding benefits.

By confirming the finding of the Commission that the equities of the unsecured creditors and the stockholders are without value, based on an estimate of future earnings, an estimate at best shrouded in uncertainty, the court, by judicial fiat, has forever forfeited and destroyed the rights and interests of such creditors and stockholders in the assets of the debtor, a result which, under well-settled principles, a court of equity will ordinarily avoid.

It may be urged that the elimination of the stock will provide the debtor with a stronger financial structure and enable it to better serve the public interests, but private property cannot be taken in the public interest without just compensation.

Even if viewed solely from the standpoint of future earnings, it would seem that it should not be said such stock is without value merely because, during periods of receding economy and depression, the earnings of the debtor will not be sufficient, after payment of prior claims, to provide funds from which dividends on such stock can be properly paid. Such stock has value, if, during periods of expanding economy and property, the earnings of the debtor will be sufficient to provide for prior claims and leave a surplus from which substantial amounts can be lawfully paid as dividends thereon; and a finding of no value should not be made if there is reasonable probability that earnings will be realized from which substantial dividends can be paid, even though only during periods of economic prosperity.

[fol. 267] It seems to me, under the facts presented on this record and those of which we may take judicial notice, that it is not unlikely the estimate of future earnings of the debtor made by the Commission will fall far short of its actual future earnings. Should the estimated earnings prove to be substantially under the actual earnings, the injustice that will result to the holders of the general mortgage bonds and to the stockholders of the debtor is obvious.

It may be reasonably assumed that a substantial portion of the war industries contributing traffic to the road will be succeeded by permanent industries. For example, it is common knowledge that the Kaiser Industries and one of the large Eastern steel companies have indicated a desire to acquire and continue the operation of the Geneva Steel Plant, a large and modern steel plant built on the debtor's line of railroad. In the areas tributary to debtor's line of railroad, there is an abundance of cheap power and of fuel and ore. Many heavy traffic producing enterprises have been and are being established in new areas tributary to the debtor's line of railroad. It is reasonable to believe that this industrial development will continue.

Furthermore, changes in national income at constant prices have an approximately constant relationship to changes in ton-miles of traffic. It may be said, in general, that traffic is so related to national income that when that income rises by one billion dollars, traffic rises by about 6.6 billion ton-miles. Certain federal agencies have made estimates of the national income for the years 1947 to 1949. These estimates predict a national income of approximately 135 billion dollars in 1947 and a rising national income in 1948 and 1949, reaching 150 billion dollars in the latter year.[3] This would indicate a postwar railroad traffic reaching in 1949 a level of that traffic during 1943.

Moreover, the ratio between ton-mile revenue of Class I railroads and the number of factory workers engaged in the [fol. 268] production of durable goods is fairly constant. It is 100,000 revenue ton-miles for each factory worker. That there will be a determined effort to provide jobs for upward of 55 million workers early in the postwar period is a well-known fact. This indicates a greatly increased postwar railroad traffic. Moreover, the record demonstrates that, with the exception of a slight dip in 1923, the debtor has been securing a constantly increasing proportion of the operating revenues of Class I railroads. If the debtor should enjoy postwar earnings approximating its 1943 earnings, it is clear that the valuation found by

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[3] See Post-War Traffic Levels, prepared by Spurgeon Bell, Head Transport Economist, and L. E. Peabody, Principal Transport Economist, of the Interstate Commerce Commission, pp. 42-71, 90-114.

the Commission should be substantially increased. But, as suggested above, it is my conclusion that only through corrective legislation or a more liberal attitude on the part of the Commission can the junior security holders obtain relief.

[fol. 269] In United States Circuit Court of Appeals

Judgment—May 10, 1945

These causes came on to be heard on the transcript of the record from the District Court of the United States for the District of Colorado and were argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the order of the District Court of October 25, 1943, approving the plan, and its order of November 29, 1944, confirming the plan, are hereby reversed and the cause is remanded with directions to enter an order disapproving the plan, and remanding the case back to the Interstate Commerce Commission for its further consideration; and that appellants have and recover of and from appellees their costs herein.

[fol. 270] In United States District Court

Oral Opinion—Hearing had on September 14, 1943

"The Court: It seems to the Court that the recent decisions of the Supreme Court have not dealt specifically with what is to be done with the surplus cash resulting from the great increase in business that the railroads of this country have experienced during the war period.

This railroad has an amount of cash here that it is not necessary to carry forward into the reorganization; it is not necessary for the proper financing of the new company, and even if this two million dollars plus is paid, there would still be plenty of working capital to go ahead with under the plan.

I have old-fashioned ideas, perhaps, and in all receiverships in this court, where there are debts and assets to pay them, I believe in paying off one's debts; that that is the best financing there is.

I see nothing in the statute or in the plan which forbids this action. It has been admitted that the Court could have [fol. 271] paid this off before the plan came out, and I am not

convinced that the simple fact that the plan has been promulgated changes that situation, or the power of the Court to deal with this surplus cash.

My experience with this railroad in its previous receiverships indicates that if too much cash is turned over to the new company, it will be used not for the payment of debts but for the interests of the security holders or the public.

So the order of the Court will be that these Rio Grande Junction Bonds be paid, with interest. The amount would be a matter of accounting, and if counsel cannot agree upon that, the Court will discuss it later with them. But I believe that this two million dollars plus of bonds should be paid off, and an order to that effect may be made.

I believe the remedy for any complaint against the Court's action is by appeal, and I do not believe it requires the Court to send the plan back to the Commission of its own motion.

The railroads of America are being watched very carefully to see what disposition will be made of these tremendous earnings and surpluses that they are building up. If they are used wisely and providently for the purpose of reducing their heavy load of indebtedness, all will be well; otherwise they invite more radical legislation of a nature that will affect the railroad security holders to a far greater degree than any plan that the Commission or the Court can compel them to take.

Mr. Gibson: If the Court please, with that ruling and order, may I ask your Honor whether you would consider reaching that result by way of purchase rather than a payment, in order to avoid serious income taxes?

The Court: Yes, you may make the order in any way so that it will avoid taxes or most convenient in considering these incidental questions that may arise. I shall be glad to consider it when the order is drawn. Is there anything else before we get down to the plan?

[fol. 273] IN UNITED STATES DISTRICT COURT

ORDER (No. 484) FOR PURCHASE OF JUNCTION BONDS—Filed September 16, 1943

This matter came on further to be heard at this term, and was argued by counsel, and, thereupon, upon consideration thereof, it was

ORDERED:

1. The Trustees of the Debtor, The Denver and Rio Grande Western Railroad Company, are hereby directed, out of the cash funds in their hands as Trustees, to purchase for the benefit of the trust estate the First Mortgage 5% Bonds due December 1, 1939 of The Rio Grande Junction Railway Company, at the principal amount thereof and the unpaid interest thereon computed at the rate of 5% per annum to the date when funds are made available for such purchase.

2. Said Trustees are directed to give not less than two weeks' notice of the time and place at which holders of said Bonds may present their Bonds for sale to such Trustees, and of the terms thereof, by publishing at least once in a newspaper published and of general circulation in the City of Denver, Colorado and at least once in one or more newspapers published and of general circulation in the City of New York, New York a notice in substantially the following form:

> "To Holders of The Rio Grande Junction Railway Company First Mortgage 5% Bonds due December 1, 1939;
>
> NOTICE is hereby given that, pursuant to order of the U. S. District Court for the District of Colorado, the undersigned will, on and after ——, 1943, purchase the above-described bonds, at the price of $— per $1,000 bond, such price representing the principal [fol. 274] amount of each of said bonds, together with interest thereon from June 1, 1935 to ——, 1943 computed at the rate of 5% per annum.
>
> Holders of said bonds may deliver the same and receive the purchase price, on or after ——, 1943, at the office of Central Hanover Bank and Trust Company, 70

Broadway, New York (as agent of the Trustees), or at the office of the Trustees in Denver, Colorado, bonds in coupon form to be accompanied by the coupons maturing on December 1, 1935 and subsequently, and registered bonds to be accompanied by duly executed instruments of transfer.

Wilson McCarthy, Henry Swan, Trustees of The Denver and Rio Grande Railroad Company."

3. The said Trustees shall hold said Rio Grande Junction Railway Company First Mortgage 5% bonds, when acquired by them, subject to the further order or orders of the Court, and the Court reserves full jurisdiction to determine the disposition to be made of such bonds and of all interests therein, and of all questions arising from their acquisition.

J. Foster Symes, United States District Judge.

Denver, Colorado, September 16th, 1943.

[File endorsement omitted.]

[fol. 275] In United States District Court

Certificate of Interstate Commerce Commission—Filed July 15, 1944

Interstate Commerce Commission, Washington

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company Reorganization

Summary of Certificate

July 4, 1944.

Pursuant to its order of March 23, 1944, the Commission, division 4, on April 26, 1944, submitted for acceptance or rejection by creditors of classes 6, 7, 8, 10(a), 10(b), 11, 12(a), and 12(b) of The Denver and Rio Grande Western Railroad Company, and by creditors of classes 1 and 2 of The Denver and Salt Lake Western Railroad Company,

as therein provided, the plans of reorganization of The Denver & Rio Grande Western Railroad Company, debtor, and of The Denver and Salt Lake Western Railroad Company, subsidiary debtor, approved by the Commission by its third supplemental report and order of June 14, 1943, and approved by the District Court of the United States for the District of Colorado on October 25, 1943. The results of the voting on the basis of the principal and interest of the claims voted, are summarized in the following tabulation,

Class	Per cent of Total Vote Accepted	Rejected
6. Holders of The Denver & Rio Grande Railroad Company's first consolidated bonds	99.29	0.71
7. Holders of The Rio Grande Western Railway Company's first-trust mortgage bonds	99.74	0.26
8. Holders of The Rio Grande Western Railway Company's first consolidated mortgage bonds	99.53	0.47
10(a) Holders of the debtor's refunding and improvement mortgage bonds (Series A)	80.00	20.00
10(b) Holders of the debtor's refunding and improvement mortgage bonds (Series B)	95.88	4.12
11. Holders of the debtor's general mortgage bonds	20.67	79.33
12(a) Reconstruction Finance Corporation; holder of debtor's secured notes	100.00	
12(b) Chase National Bank of the City of New York, holder of debtor's secured note	100.00	
1. Holder of The Denver and Salt Lake Western Railroad Company's common stock	100.00	
[fol. 276] 2. Reconstruction Finance Corporation, holder of The Denver & Salt Lake Western Railroad Company's secured note	100.00	

[fol. 277] Certificate

At a Session of the Interstate Commerce Commission, Division 4, held at its office in Washington, D. C., on the 4th day of July, A. D. 1944.

Finance Docket No. 14002

The Denver and Rio Grande Western Railroad Company
Reorganization

The Commission, division 4, having on April 26, 1944, pursuant to its order of March 23, 1944, in this proceeding, submitted for acceptance or rejection by creditors of classes 6, 7, 8, 10(a), 10(b), 11, 12(a), and 12(b) of The Denver and Rio Grande Western Railroad Company, and by creditors of classes 1 and 2 of The Denver and Salt Lake Western Railroad Company, as therein provided, the plans of reorganization of The Denver and Rio Grande Western Railroad Company and of The Denver and Salt Lake Western Railroad Company approved by the Commission by its third supplemental report and order of June 14, 1943, and approved by the District Court of the United States for the District of Colorado having jurisdiction of the proceedings for reorganization of the debtor, by order of October 25, 1943.

It is hereby certified, That proper ballots for acceptance or rejection of the plan were transmitted, within the time specified in the order of March 23, 1944, by creditors of class 6, holding $21,739,000, principal amount, of The Denver & Rio Grande Railroad Company first consolidated mortgage bonds, out of a total of $40,507,000, principal amount, of such bonds outstanding; by creditors of class 7, holding $9,499,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds, out of a total of $15,190,000, principal amount, of such bonds outstanding; by the creditors of class 8, holding $9,166,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds, out of a total of $15,080,000, principal amount, of such bonds outstanding; by the creditors of class 10(a), holding $1,000,000, principal amount; of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage six-percent series A bonds, out of a

total of $2,000,000, principal amount, of such bonds outstanding; by the creditors of class 10(b), holding $4,500,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage five-percent bonds, series B, out of a total of $12,000,000, principal amount, of such bonds outstanding; by the creditors of class 11, holding $6,443,150, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds, out of a total of $29,808,000, principal amount, of such bonds outstanding; by the Reconstruction Finance Corporation, sole creditor of class 12(a), holding secured notes of The Denver and Rio Grande Western Railroad Company in the principal amount of $7,581,000; by the Chase National Bank of the City of New York, sole creditor of class 12(b), holding a secured note of The Denver and Rio Grande Western Railroad Company in the principal amount of $1,500,000; by the trustees of The Denver and Rio Grande Western Railroad Company, voting as representatives of that company as sole stockholder of class 1 of The Denver and Salt Lake Western Railroad Company, for the entire outstanding 36,310 shares of common stock of that company; and by [fol. 278] the Reconstruction Finance Corporation as sole creditor of class 2 of The Denver and Salt Lake Western Railroad Company, holding a secured note of that company in the principal amount of $3,110,850.

It is further certified, That defective ballots, hereinafter more specifically described, were transmitted within the time specified in the order of March 23, 1944, by other creditors of class 6, holding $355,500, principal amount, of The Denver & Rio Grande Railroad Company first consolidated mortgage bonds; by other creditors of class 7, holding the $138,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds; by other creditors of class 8, holding $38,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds; by other creditors of class 10(b), holding $382,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage bonds, series B; and by other creditors of class 11, holding $287,200, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds outstanding.

It is further certified, That creditors of class 6, holding $21,585,000, principal amount, of The Denver & Rio Grande Railroad Company first consolidated mortgage bonds, constituting (with accrued interest) 99.29 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that creditors of that class holding $154,000, principal amount, of the bonds, constituting (with accrued interest) 0.71 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 7, holding $9,474,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds, constituting (with accrued interest) 99.74 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that creditors of that class holding $25,000, principal amount, of the bonds, constituting (with accrued interest) 0.26 percent of the total of allowed claims of that class voting on the plan rejected the plan.

It is further certified, That creditors of class 8, holding $9,123,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds, constituting (with accrued interest) 99.53 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $43,000, principal amount, of the bonds, constituting (with accrued interest) 0.47 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 10(a), holding $800,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage six-percent series A bonds, constituting (with accrued interest) 80.0 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $200,000, principal amount, of the bonds, constituting (with accrued interest) 20.0 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 10(b), holding $4,401,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and im-
[fol. 279] provement mortgage five-percent series B bonds, constituting (with accrued interest) 95.88 percent of the

total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $189,000, principal amount, of the bonds, constituting (with accrued interest) 4.12 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 11, holding $1,332,050, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds, constituting (with accrued interest) 20.67 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $5,111,100, principal amount, of the bonds, constituting (with accrued interest) 79.33 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That the Reconstruction Finance Corporation, sole creditor of class 12(a), holder of The Denver and Rio Grande Western Railroad Company secured notes in the principal amount of $7,581,000 and interest accrued and unpaid as of January 1, 1943, amounting to $2,928,778.31, constituting 100 percent of the total of the allowed claims for that class, accepted the plan.

It is further certified, That the Chase National Bank of the City of New York, sole creditor of class 12(b), holder of The Denver and Rio Grande Western Railroad Company secured note in the principal amount of $1,500,000 and interest accrued and unpaid as of January 1, 1943, amounting to $658,458, constituting 100 percent of the total of the allowed claim for that class, accepted the plan.

It is further certified, That Wilson McCarthy and Henry Savan, as trustees for The Denver and Rio Grande Western Railroad Company, sole stockholder of Class 1, of The Denver and Salt Lake Western Railroad Company, holder of 36,310 shares of the common stock of that company, constituting 100 percent of the total of the allowed claim for that class, accepted the plan.

It is further certified, That the Reconstruction Finance Corporation, sole creditor of class 2, of The Denver and Salt Lake Western Railroad Company holder of a secured note of that company in the principal amount of $3,110,850 and interest accrued and unpaid as of January 1, 1943, amounting to $1,179,976.64, constituting 100 percent of the total of the allowed claim for that class, accepted the plan.

It is further certified, That creditors of class 6, holding $355,500, principal amount, of The Denver & Rio Grande Railroad Company first consolidated bonds, constituting (with accrued interest) 0.88 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) Five ballots, representing $23,000, principal amount, of the bonds, which failed to show whether the ballots were intended for acceptance or rejection of the plan.

[fol. 280] (2) Sixteen ballots for acceptance of the plan (14 of which represented $162,500, principal amount, of the bonds,) which failed to show the serial numbers of the bonds. Two of these ballots also failed to show the principal amount of the bonds.

(3) Ten ballots for acceptance of the plan, representing $30,000, principal amount, of the bonds, which were not supported by documentary evidence of authority to execute the ballots.

(4) Twenty ballots for acceptance of the plan, representing $140,000, principal amount, of the bonds, on which the signatures of the claimants were not witnessed.

It is further certified, That creditors of class 7, holding $138,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds, constituting (with accrued interest) 0.91 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) Thirteen ballots for acceptance of the plan, representing $98,000, principal amount, of the bonds, which were not supported by documentary evidence of authority to execute the ballots.

(2) Five ballots for acceptance of the plan, representing $30,000, principal amount, of the bonds,

on which the signatures of the claimants were not witnessed.

(3) One ballot for acceptance of the plan, representing $10,000, principal amount, of the bonds, which failed to show the serial numbers of the bonds.

It is further certified, That creditors of class 8, holding $38,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds, constituting (with accrued interest) 0.25 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) One ballot for rejection of the plan, representing $1,000, principal amount, of the bonds, which failed to show the serial number of the bond.

(2) Five ballots for acceptance of the plan, representing $31,000, principal amount, of the bonds, on which the signature of the claimants were not witnessed.

(3) One ballot for acceptance of the plan, representing $3,000, principal amount, of the bonds, which was not supported by documentary evidence of authority to execute the ballot.

(4) One ballot, representing $3,000, principal amount of the bonds, which failed to show whether the ballot was intended for acceptance or rejection of the——

[fol. 281] *It is further certified*, That creditors of class 10(b), holding $382,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage bonds, series B, constituting (with accrued interest) 3.18 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) One ballot, representing $4,000, principal amount, of the bonds, which failed to show whether the ballot was intended for acceptance or rejection of the plan.

(2) Five ballots for acceptance of the plan, representing $59,000, principal amount, of the bonds, and one ballot for rejection of the plan, representing $4,000, principal amount, of the bonds, which failed to show the serial numbers of the bonds.

(3) Seven ballots for acceptance of the plan, representing $60,000, principal amount, of the bonds, and one ballot for rejection of the plan, representing $5,000, principal amount, of the bonds, on which the signatures of the claimants were not witnessed.

(4) One ballot for acceptance of the plan, representing $35,000, principal amount, of the bonds, and five ballots for rejection of the plan, representing $215,000, principal amount, of the bonds, on which the serial numbers of the bonds were incorrect.

It is further certified, That creditors of class 11, holding $287,200, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds, constituting (with accrued interest) 0.96 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) Three ballots, representing $17,000, principal amount, of the bonds, which failed to show whether the ballots were intended for acceptance or rejection of the plan.

(2) One ballot for acceptance of the plan, representing $3,000, principal amount, of the bonds, which was not supported by documentary evidence of authority to execute the ballot.

(3) Three ballots for acceptance of the plan, representing $111,000, principal amount, of the bonds, and four ballots for rejection of the plan, representing $99,700, principal amount, of the bonds, which failed to show the serial numbers of the bonds.

(4) Nine ballots for acceptance of the plan, representing $36,000, principal amount, of the bonds, and two ballots for rejection of the plan, representing $20,500, principal amount, of the bonds, on which the signatures of the claimants were not witnessed.

[fols. 282-283] *And it is further certified*, That the following ballots, more specifically described below, were received or were postmarked after the close of the voting period specified in the order of March 23, 1944, and, therefore, were not counted either with those of creditors who submitted proper ballots for acceptance or rejection of the plan, or with those of creditors whose ballots were deemed defective for the reasons hereinbefore stated:

Class 6. The Denver and Rio Grande Railroad Company first-consolidated bonds

(1) Eighteen ballots for acceptance of the plan, representing $134,000, principal amount, of the bonds, and one ballot for rejection of the plan, representing $10,000, principal amount, of the bonds.

Class 7. The Rio Grande Western Railway Company first trust mortgage bonds

(1) One ballot for acceptance of the plan, representing $5,000, principal amount, of the bonds.

Class 8. The Rio Grande Western Railway Company first consolidated mortgage bonds

(1) Three ballots for acceptance of the plan representing $6,000, principal amount, of the bonds.

Class 10(b). The Denver and Rio Grande Western Railroad, Company refunding and improvement mortgage bonds, series B

(1) Three ballots for acceptance of the plan, representing $150,000, principal amount, of the bonds.

Class 11. The Denver and Rio Grande Western Railroad Company general mortgage bonds

(1) Four ballots for acceptance of the plan, representing $11,000, principal amount of the bonds, and one ballot for rejection of the plan, representing $5,000, principal amount, of the bonds.

the Commission, division 4.

W. P. Bartel, Secretary.

A true copy:

W. P. Bartel, Secretary of the Interstate Commerce Commission. (Seal.)

[File endorsement omitted.]

[fol. 284] IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO, SITTING AT DENVER

No. 8669

In the Matter of The Denver and Rio Grande Western Railroad Company, Debtor

In Proceedings for Reorganization of a Railroad

HEARING ON CONFIRMATION OF PLAN AND PETITION OF CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE OF THE GENERAL MORTGAGE, FOR CONSTRUCTION OF THE PLAN AND FOR OTHER RELIEF—Filed January 10, 1945

Be it remembered that on, to wit, the 30th day of August, A. D. 1944, the same being one of the regular juridical days of the May Term, A. D. 1944, of said court, this cause came on for hearing before the Honorable J. Foster Symes, Judge of the District Court of the United States for the Judicial District of Colorado.

APPEARANCES:

Henry McAllister, Esq., for the Trustees of the debtor, The Denver and Rio Grande Western Railroad Company.

William V. Hodges, Esq., of the firm of Hodges, Vidal & Goree, for the debtors The Denver and Rio Grande Railroad Company and the Denver and Salt Lake Railroad Company.

Messrs. George D. Gibson, of the firm of Hunton, Williams, Anderson, Gay & Moore, and Morrison Shafroth, of the firm of Grant, Shafroth & Toll, for the Insurance Group Committee.

[fol. 285] Messrs. Edwin S. S. Sunderland of the firm of Davis, Polk, Wardwell, Sunderland & Kiendl, and Robert G. Bosworth of the firm of Pershing, Bosworth, Dick & Dawson for the Guaranty Trust Company of New York, as Trustee.

Messrs. Edward E. Wafts, Jr., of the firm of Mitchell, Capron, Marsh, Angulo & Cooney, and Milton J. Keegan, of the firm of ~~Dines, Dines & Holme~~, for City Bank Farmers Trust Company, as Trustee.

Messrs. James L. Homire and James A. March for the Reconstruction Finance Corporation.

Erskine R. Myer, Esq., for H. Allyn Hicks, Esq., Trustee of the debtor The Denver and Salt Lake Western Railroad Company.

Langdon H. Larwill, Esq., of the firm of Lindsay & Larwill, for the United States Trust Company of New York, as Trustee.

Messrs. William L. Cohn and J. F. Schneider for the Untermeyer Family Group.

Henry H. Larimore, Esq., for Guy A. Thompson, Esq., Trustee of the Missouri Pacific Railroad Company.

Miss Norma L. Comstock for the Central Hanover Bank and Trust Company, as Trustee.

Thereupon the following proceedings were had:

The Court: We have several matters this morning. Can anyone suggest in what order we should take them up? First is the petition of the City Bank Farmers Trust Company as Trustee of the General Mortgage, for construction of the plan and for other relief, and the objection of the debtors, that is, the Denver and Rio Grande—that same objection, and the objections of the City Bank Farmers Trust Company, and the objections of the Missouri Pacific Railroad Company.

Mr. Keegan: If the Court please, the City Bank Farmers Trust Company's petition asks for an adjustment within the framework of the plan as a result of the purchase of the Junction bonds. That particular issue doesn't go to any change or increase in capitalization. It is separate and distinct from the other issues. We have also raised that same point in our objections to the confirmation, asking that this adjustment be made as a matter precedent to the confirmation. We suggest that that narrower issue be heard first. We would like to ask Mr. Thompson a few questions going to that particular issue.

The Court: If there is no objection we will take that matter up first.

Mr. Keegan: If nobody wants to make any further statement I would like to call Mr. Thompson. He is here.

Thereupon the City Bank Farmers Trust Company, to maintain the issues herein on its behalf, offered and gave in evidence as follows:

T. A. Thompson, being called and sworn as a witness on behalf of the City Bank Farmers Trust Company, testified as follows:

Direct examination.

By Mr. Keegan:

Q. Your name is Mr. T. A. Thompson?

A. Yes, sir.

Q. You are the General Auditor for the trustees of The [fol. 287] Denver and Rio Grande Western Railroad Company?

A. I am.

Q. Mr. Thompson, after the Court entered its order last September for the trustees out of cash funds in their hands to purchase the Rio Grande Junction Railway Company First Mortgage bonds, how many of these bonds were purchased by the trustees by December 31, 1943?

A. $1,936,000.00 principal amount.

Q. Will you please state the amount of the cash outlay the trustees used in purchasing the Junction bonds?

A. Approximately $2,750,000.00.

Q. Will you please state the approximate amount of these Junction bonds which have been purchased by the trustees to date?

A. As of July 31st $1,977,000.00.

Q. That is principal?

A. Principal.

By the Court:

Q. What is that difference between that and $2,750,000.00; is that interest?

A. The $2,750,00.00 includes the interest figured on the price of the bonds.

Q. What year?

A. Actually from June 1, 1935—to July 1, 1935—I will get it right after awhile—to September of last year it was—November 1st.

By Mr. Keegan:

Q. Now, of the bonds the trustees have purchased up to July 31st will you state approximately how much they paid

for those, including principal and interest?

A. $2,809,000.00.

Q. This leaves how many Junction bonds still to be purchased?

A. Twenty-three thousand in principal amount for which the price will be approximately $32,679.00.

Q. Will your please state the amount of cash and government bonds that the trustees had on hand January 1, [fol. 288] 1943, the effective date of the plan?

A. $10,850,000.00.

Q. Will you state the amount of cash and government bonds that the trustees had on hand at the date of the hearing on the Commission's plan before this Court last September 16, 1943?

A. $20,000,000.00.

Q. Will you please state the amount of cash and government bonds on hand at the close of last year, December 31, 1943?

A. $20,724,000.00 plus government bonds or cash set aside for deferred maintenance in the amount of $3,751,995.00.

Q. And how much cash and government bonds do you have on hand at the present time, or the nearest date?

A. $17,575,000.00 plus the maintenance fund.

Q. That is plus the $3,751,995.00?

A. That is correct.

Q. Will you please state the amount of the excess of current assets over current liabilities?

A. On January 1, 1943, approximately $7,700,000.00.

Q. Will you please state the amount of the current assets over current liabilities on September 16, 1943?

A. Approximately $12,500,000.00.

Q. On December 31, 1943?

A. $10,400,000.00.

Q. At the present time or at the nearest to the present time you have the figures?

A. As of June 30th $10,850,000.

Q. Mr. Thompson, I hand you some exhibits that have been marked for identification as C. B. F. T. Co. Exhibits Nos. 1 to 8, inclusive. Will you please examine those. Now, Exhibits 1 to 7 are printed Income Account Statements for July, 1943, August, 1943, September, 1943, December, 1943, March, 1944, April, 1944, and July 1944. Exhibit 8

is labeled printed, "Report of The Denver and Rio Grande Western Railroad Company, Wilson McCarthy and Henry Swan, Trustees, Year Ended December 31, 1943." Were [fol. 289] those reports prepared by you or under your supervision?

A. They were.

Mr. Keegan: I would like to offer those in evidence, your Honor.

The Court: They will be admitted if there is no objection.

Mr. Keegan: I have two or three more questions I would like to ask Mr. Thompson.

Q. I call your attention to page 32 of Exhibit 8 which is the 1943 annual report.

Mr. Keegan: Mr. Gibson has asked that on those monthly income account statements, to make the record complete, that we start in with the month of July, 1943, and make it complete every month to date, and we have no objection to that, and if it is agreeable to the Court Mr. Thompson can bring over those other income statements and introduce them a little later. Will that be agreeable?

By the Court:

Q. Are these the regular monthly account statements?

A. Yes, they are.

The Court: Very well.

By Mr. Keegan:

Q. Mr. Thompson, I call your attention to page 32 of Exhibit 8, which is the 1943 annual report. Can the debtor's income available for interest on the funded debt and on that part of the unfunded debt covered by the Reconstruction Finance Corporation loan and the Chase National Bank loan in each year from 1935 to 1943, inclusive, be computed from the figures shown on page 32 of Exhibit 8?

A. They can in short.

[fol. 290] Q. How should those computations be made?

A. Take the first block and take the amount shown as available for interest on funded debt, add into it the columns 2 and 4 covering the RFC loan and the bank loans.

Q. Can the debtor's interest requirements for securities senior to the General Mortgage bonds, including interest on the RFC loan and the Chase National Bank loan for the years from 1935 to 1943, be computed from the figures on this page 32?

A. They can.

Q. How should this computation be made?

A. Well, the shortest method would be to take the $5,208,000.00 and corresponding figures for the previous year in the first column of block 2, add the columns 2 and 4 in block 1 and deduct the $1,490,400.00 shown as General Mortgage interest.

Q. That is column 5 in block 2?

A. Column 6.

Q. Mr. Thompson, I call your attention to Income Account Report for the month of July, 1944, page 2 I believe it is. Does that page show the debtor's income available for interest for the first seven months of this year?

A. It does.

Q. How much?

A. $5,992,836.00.

Q. I call your attention to page 5 in this Exhibit 7. Can the debtor's interest requirement for the securities senior to the General Mortgage for the first seven months of this year be computed from the figures on page 5?

A. They can.

Q. How should that computation be made?

A. Well, the last block of figures on page 5 covers all the interest. Deducting from the $3,411,000.00 the amount of interest shown under "Interest on General Mortgages" of $869,400.00.

Mr. Keegan: Those are all the questions I have of Mr. Thompson.

[fol. 291] Mr. Gibson: May it please the Court, before cross-examination of this witness begins, may it be understood, for I think it would simplify the hearing if it can, that the testimony of this witness will be applicable not only to the City Bank Farmers Trust Company, but also to the confirmation of the plan?

The Court: We will consider it on any question that it is material on. Go ahead with your cross-examination.

Cross-examination.

By Mr. Gibson:

Q. Mr. Thompson, you said that the net available for interest for the first seven months of 1944 was a figure of slightly less than $6,000,000.00. Could you tell us what the corresponding figure was for 1943?

A. $10,286,470.00.

Q. Has that adverse relation of 1944 to 1943 been reversed at the present time?

A. I don't think I understand your question.

Q. Six million dollars were reported as available for interest in the first seven months of 1944 as against $10,000,000.00 in the corresponding months of 1943. That is what I meant by adverse relation. Has that relation been changed since the last report you put in evidence?

A. Well, the figures speak for themselves.

Q. Well, I am asking you to supplement the figures you have put in evidence so far as you can. Are you doing better now than you were in 1943, or worse?

A. Definitely worse.

Q. Does that apply to gross revenues as well as net?

A. Not a substantial degree by any means. The loss in gross for the first seven months is $956,000.00.

[fol. 292] Q. It has been that much less for 1944 as against 1943?

A. That is correct.

Q. Could you give us the figures for the last available period? If that is a weekly period give us the last available week and the last available month, or all the available periods for July.

A. This is through July, Mr. Gibson. We have estimated figures through August 21st of gross only. I don't have those figures with me.

Q. I think it will be sufficient if you will give us the percentage of decline in each of the three periods that are most recently reported.

A. For the period ending August 21st the week shows a decline of 8.79 per cent. The month shows a decline of 5.45 per cent, and the year a decline of 2.74 per cent.

Q. Thank you very much. When you said that from page 32 of the 1943 annual report a calculation could be made of interest on the Chase bank notes and the Reconstruction

Finance Corporation notes I take it you were referring to the stipulated interest on the notes themselves, and not to the collateral. Is that correct?

A. That is correct.

By the Court:

Q. Have you any figures showing the decline in carloadings represented by that loss in gross?

A. Not with me. I can get them on very short notice. I happen to know the decline in carloads was substantially the figure in revenue.

By Mr. Honnire:

Q. Does that decline in loads occur in both government and commercial?

A. Our biggest loss is in bridge traffic which is predominantly government business.

Q. It is due to war operations at this time?

A. Yes sir.

[fol. 293] By the Court:

Q. What is your gross business deficiency?

A. Fifty, fifty-five, probably sixty per cent. I am speaking of bridge traffic.

Q. I mean gross traffic.

A. I wouldn't be surprised if that was fifty per cent.

Q. Would it be that much in gross, government and general business?

A. Approximately thirty-five.

By Mr. Homire:

Q. What is the status of the land grant rates with relation to government business? Is that in a state of controversy?

A. So far as the Rio Grande is concerned there is no direct controversy. We are seriously involved as an intermediate carrier, and the settlements are made in our case by the terminal lines and the majority of it by the western lines. Therefore we are unable to do anything but guess as to the amount that could be involved in those disputes.

Q. Should those disputes result in an adverse decision to the railroads, what effect would that have on the cash position of the Rio Grande?

A. It would mean we would have in effect to give back cash or reduce our current remittances in the amount of the land grant deductions.

Q. They might be very considerable if that question was resolved against the railroads?

A. They could be substantial.

By the Court:

Q. In these cash balances, have you taken into consideration the deductions allowed for income taxes?

A. The bonds include bonds purchased to pay income taxes.

Q. Have you paid all your income taxes up to date?

[fol. 294] A. Federal income.

Q. Would that be the figures you have given? Would the balance of the cash available be affected?

A. There is approximately $3,500,000.00 in taxes due at this time. That is for the balance of this year plus the current year's accumulation.

Q. You haven't deducted that from the balance you have given?

A. We have not.

By Mr. Keegan:

Q. In other words, in your excess of current assets over current liabilities, it is in there and not taken out?

A. Yes.

Mr. Gibson: There is one question I overlooked, if your Honor please.

By Mr. Gibson:

Q. In the annual report to stockholders for 1943 that you introduced in evidence, Mr. Thompson, at page 5 a summary is given of the increases in wages to employees, and that discussion concludes with the statement about the middle of page 5: "It is estimated, on basis of present force, that the increases now in effect"—those are increases in wages—"on an annual basis, will amount to $2,700,000." I would like to ask whether that statement is still substantially representative of the existing situation?

A. I believe it is accurate as any we could make even to date.

By the Court:

Q. Does that mean that much additional will have to be paid out on the cash basis?

A. No, that would mean the normal pay roll costs 1944 over 1943 prior to the wage increases. 1943 expenses include in them as much of the retroactive pay as we could possibly see at the time we closed the report.

[fol. 295] By Mr. Hodges:

Q. Mr. Thompson, you have testified that there has been paid out approximately $2,800,000.00 to take up the Junction bonds?

A. Correct.

Q. And you have given us the figure for the amount that was paid in the year 1943. Did you consider the charging of that amount to the operating expenses of the gross operation?

A. No. We are carrying it in the trustees' investment account.

Q. You didn't so charge it?

A. I did not.

Q. And you have also paid out a considerable sum in this year, 1944, for the acquisition of further amounts of those bonds, and that has not been charged as a part of the operating expenses of the gross proceeds?

A. That is correct.

Q. Now, Mr. Thompson, have you with you the data showing the analysis of the traffic of this road on which you base an estimate of thirty-five per cent government business?

A. I don't have it with me. I happen to know that our government business amounts to 10,000 to 12,000 carloads a month out of a total——

Mr. Homire: The witness testified fifty per cent rather than thirty-five per cent.

The Witness: My last figure was thirty-five per cent of all traffic.

By Mr. Homire:

Q. Fifty per cent of bridge traffic?

A. That is right.

(Last question and answer read.)

A. (Continuing:) Out of a total of approximately thirty thousand cars per month.

[fol. 296] By Mr. Hodges:

Q. That data from which you deduced that statement is available, is it not?

A. It is available, but I don't like to put it in the record.

Q. I wouldn't think you would. I would like to take time to see it, and maybe recall you, but I would like to see it and go over it with you, and see on what factual basis your opinion is based.

A. All right.

Mr. Hodges: Of course, I call the attention of the Court to the fact that the factual basis should be here as distinguished from his opinion.

Q. I hold here, Mr. Thompson, the published balance sheet of December 31, 1943, and I am looking at current assets and current liabilities. Have there been any adjustments made in the figures shown on that report since the report was authenticated and issued?

A. Nothing in the way of adjustments, but we make our balance sheet monthly of course, and file it with the Court.

Q. I don't believe my question is clear to you. In looking at your reports for 1942 as of December 31st, and then looking at the recapitulation of that report or the restatement of those figures in your report of December 31, 1943, I find that there are some differences in figures, and I assume that even after you made your annual report you had to make some adjustments. Do you recognize that any adjustments were made in the report of 1942, for the year ending December 31, 1942?

A. Offhand I do not recognize any.

Q. Well, you are certain, then, that we can take the report of December 31, 1943, as a correct report, and not subject to adjustments for the period represented by that report?

[fol. 297] A. I think you can.

Q. In fairness to you and to myself if I have made a mistake about adjustments in 1942, I will take time afterwards to look at that again. I thought I saw some substantial adjustments, and I may be mistaken. Now, did the accident

in the tunnel on the Salt Lake line affect your business for 1943?

A. Substantially, yes.

Q. When was that traffic resumed?

A. On December 1, 1943.

Q. So it has not affected your 1944 traffic, or are you prepared to say whether it has or not?

A. Well, I can only say to the extent that diversions made against us during that period may have been partially continued. I don't know.

Q. That was an interruption in the ordinary relationships with the patrons of the road?

A. Substantially.

Q. And, as a matter of fact, it involved a considerable loss in 1943, did it not?

A. It materially affected our operating results for 1943.

Q. Have you ever actually figured out what loss that represented in the year 1943?

A. It can't be figured.

Q. That is one of the things that can't be figured?

A. It can be guessed at, but that is all.

Q. Well, can you figure any more definitely what part of your traffic is government traffic and what is not?

A. No.

Q. That is an estimate, isn't it?

A. That is still an estimate.

Q. Who would do the figuring to determine how much damage was done to the business of this railroad of 1943 [fol. 298] by that tunnel accident?

A. I think we should all take a shot at it.

Q. And, as a matter of fact, all of you who have special knowledge concerning the effect have talked together and considered it and arrived at an approximate estimate, have you not?

A. Well, we did talk about an estimate before the tunnel was even opened, and it continued out of service for a longer period than that, and all we can do now is just to make an approximation of revenue which was lost.

Q. What you did then is to make an approximation?

A. Yes, that is right.

Q. And you can make an approximation now?

A. Yes, on the basis of diversion orders out against us.

Q. When did you begin to pay federal income and excess profits taxes?

A. We have never paid any excess profit taxes. We paid federal income in 1942.

Q. That is the first year?

A. That is the first year.

Q. Up to that time you had not paid the government anything on account of the federal income tax. Now, in 1942 how much income tax did you pay the government, the federal government? I ask you that because while I see the item of taxes paid in your annual report, I can't be sure that I can tell what was federal income tax.

A. In 1942 our accruals, which were approximately our payments, were $2,180,000.00, of which $1,700,000.00 approximately was federal income taxes.

Q. That is an accrual figure for 1942?

A. That is correct.

Q. You would have definite data, wouldn't you, as to the amount actually paid for the 1942 income taxes?

[fol. 299] A. I have the figure, yes.

Q. Well, you have said it is approximately that amount.

A. Naturally the accounts have to be closed on the accrual basis and closed long before the tax is actually figured out.

Q. I am not asking you, though, what the accrual was. I am asking what the payment was. I have seen accruals made in perfect good faith which didn't turn out to be the actual taxes paid during that year. That can be so?

A. That can be so, yes.

Q. But in your particular case you are prepared to say you accrued it with accuracy within a very few dollars one way or the other?

A. They were fairly close.

Q. And you think that in 1942 you paid $1,700,000.00 to the government for federal income taxes?

A. That is approximately the figure. The figure was somewhere between $1,600,000.00 and $1,700,000.00.

Q. At least, then, can we settle on this: that it didn't exceed $1,700,000.00?

A. That is correct.

Q. And it was not less than $1,600,000.00?

A. That is correct.

Q. Well, that is close enough for me. And if that wasn't a proper charge against the operating expenses of the debtor's trustees, your showing of net income for that year would be increased accordingly?

A. That is correct.

Q. What income tax did you pay in 1943?

A. For 1943?

Q. Yes.

A. Our return has not yet been filed. We are paying on an estimated basis of a total tax of $6,800,000.00 federal income taxes.

Q. Now, in 1943 I see accrued tax liability of $9,186,-
[fol. 300] 723.32. That is in your report of December 31st?

A. Correct.

Q. And if approximately $6,000,000.00 of that was federal income tax——

A. $6,800,000.00.

Q. $6,800,000.00?

A. That is right.

Q. That would leave something like two million three or between two million three and two million two for other taxes. What else is included in that two million?

A. Income taxes to the State of Colorado and to the State of Utah and our general ad valorem taxes.

Q. How much of that was income tax to the State of Colorado?

A. About $220,000.00.

Q. And how much was income tax to the State of Utah?

A. Approximately $150,000.00.

Q. That is about $370,000.00 more income tax than that payable to the federal government?

A. That is right.

Q. You had that same situation in 1942, did you not?

A. We did.

Q. What was your state income tax in 1942, Colorado, then Utah?

A. As I recall that, it was $200,000.00.

Q. And Utah?

A. Utah about $90,000.00.

Q. Now, while that is your accrual of income taxes, you have not paid all of that yet, have you?

A. We have paid half of Colorado, half of the federal, and none of Utah.

Q. And that payment of federal and Colorado tax that you are now speaking of is applicable to the year 1943?

A. That is correct.

Q. How near to your accrual is that actual tax?

A. For 1943?

Q. For 1943, or do you know yet?

[fol. 301] A. The total is within $10,000.00 of our accruals.

Q. So that we can take that accrual as being remarkably close to the actual tax?

A. That we are going to pay.

Q. That you are going to pay. If that tax is not a proper expense of the trustees in their operation of this property, then your 1943 income, net income, would be increased quite substantially, would it not?

Mr. Gibson: We object to that question on the ground that a purely hypothetical question has been asked if the federal government income taxes were not proper expenses. The contingency is so remote.

Mr. Hodges: My dear sir, the contingency is right on your neck right now.

The Court: Answer that yes or no.

A. Yes.

Q. And can you state the amount by which it would be so increased?

A. About $6,800,000.00 as applicable to federal. I don't know that your question included the state.

Q. I will, if I didn't include the state in the question—I will now include that.

A. Then it would increase it by the amount of accrual shown, $7,184,000.00.

Q. Now, for the income tax accruals what is the difference between the 1942 and the 1943 net income?

A. It gives a net income for both years of approximately $13,000,000.00.

Q. Now, you have accrued some income taxes for the year 1944, have you not, in the statement you have given us?

A. We have.

Q. I have not seen that. Is that all in one exhibit?

A. That is in the exhibit that has been introduced in evidence.

[fol. 302] Q. May I see a copy of that exhibit? I don't know which one it is. I will identify it in a moment. Let's see what exhibit that is.

A. Exhibit 7.

Q. Have you an extra copy of it there?

A. I have my own copy.

Q. Well, just keep it then. I will use the court copy. Now, we are talking about the accrual of income taxes, fed-

eral and state; for the period January 1 to July 31, 1944 I see it, Mr. Thompson. Railway tax accruals.

A. It gives the details in the first block on page 5.

Q. Well, I get it for the month of July, 1944, in the first column on page 5, but it is in the fifth column of the first block; is that correct?

A. That is correct.

Q. And there is an accrual of $1,675,700.00 for federal and state income taxes for the first six months of 1944?

A. For the first seven months.

Q. Or a reduction of 65.16 per cent over the same period in 1943?

A. That is correct.

Q. Now, in computing your accrual you are computing a very much lower income for 1944 than you had in 1943; is that correct?

A. That is correct.

Q. Now, in this same exhibit there is a statement of operating revenues for the same period, and I find that on page 2, and I find that there is in the last column in the first block on page 2—that there is a reduction in operating revenues of 2.38?

A. That is correct.

Q. And that the freight revenues have fallen off 3.45?

A. That is correct.

Q. Now, in the next block of operating expenses am I correct that in this period there has been an increase of [fol. 303] 54.76 per cent in maintenance of way and structures, roadway and track?

A. No, the total is 59.43 per cent.

Q. Well, now, I look at this and I read 54.76.

A. That is breakdown of the roadway and track structure alone.

Q. That is what I said.

A. Well, the bridges are a part of that too, but they are separate.

Q. That is set up in a separate block, isn't it?

A. That is correct.

Q. Bridge structures increase of 53.3?

A. That is right.

Q. Now, how do the actual expenditures for maintenance of way and structures conform to the expenditures in 1943?

A. That would require considerable analysis. Without an analysis I can't answer your question.

Q. There is someone in the organization who would have that, is there not, or would that be in your office?

A. These are the figures in our office or almost any office.

Q. Any office that had the figures?

A. That is right.

Q. Reliable as they are in your office. I will go into that a little later because that raises this question. In computing your income for 1942 did you deduct more than the normal maintenance expense?

A. 1942?

Q. Yes.

Mr. Homire: I think that is an objectionable question. We object to it because we don't know what the "normal maintenance" means.

The Court: Objection overruled. You can clear it up on cross examination.

A. I don't know of any extraordinary charges in 1942 to maintenance other than some minor charges to amortization.

Q. Well, I think we can get at it more simply by ourselves [fol. 304] taking your reports here and comparing maintenance expense for several years, without asking you specifically about this, and it will shorten it very much. Now, in arriving at your net income I see where there appears in 1942 an item "Accrued depreciation road and equipment"?

A. That is right.

Q. When was that account first introduced?

A. The figures that are used in 1942 have been in effect since 1910.

Q. Since 1910?

A. 1910 through 1942 on substantially the same basis.

Q. And this road has accrued a depreciation on equipment?

A. Equipment only.

Q. So that there really in the figures shown in 1942, $15,351,301.89 really is equipment depreciation?

A. That is correct.

Q. In these former years did you use the designation "Road and equipment," or just "Equipment"?

A. That is ICC designation—"Road and equipment." That is, depreciation of road property was optional until January 1, 1943, when it became mandatory.

Q. That is, the Commission made a ruling to that effect?

A. That is correct.

Q. And you are now following that ruling in 1943?

A. That is correct.

Q. And you have in that item in 1943 of $16,870,152.00—you have a factor which represents road depreciation as distinguished from equipment?

A. That is correct.

Q. Approximately how much is that?

A. Approximately $700,000.00.

Q. Was that determined from inspection of the depreciated property?

A. No, that is using the 1C'C formula.

[fol. 305] Q. Straight line formula?

A. That is correct.

Q. And not based upon inspection of the evidence?

A. That is correct.

Q. Now, here is another item, "Accrued amortization of defense projects equipment." When did that first come into the accounts?

A. I believe the amortization regulation came into effect January 1, 1942.

Q. So that you have an item of $743,281.78 deducted from the income of that year which you call accrued amortization of defense projects?

A. That is correct.

Q. Was that all on equipment?

A. In 1943 or 1942?

Q. 1942.

A. 1942 ninety-nine per cent of it was on equipment; a very small amount to road.

Q. Was that in addition to your equipment depreciation, the figure on the——

A. It was not. You mean used for both?

Q. But you did have in that year accrued depreciation on equipment of close to $14,750,000.00?

A. That is the accumulated figure from the date the depreciation started. The charges for the year are in the report.

Q. So that this item of amortization of defense projects is your total equipment depreciation which you deducted from earnings for that year?

A. When you speak of amortization you use your figure for depreciation.

Q. Well, let me reframe that question. You do, in arriving at your net income for that year, deduct an amortization of defense projects, do you not?

A. We do.

Q. And that applies to equipment?

A. That applies to equipment.

Q. And that is the figure shown in your 1942 report as [fol. 306] accrued amortization of defense projects?

A. Not necessarily. I say the accrued figure in the balance sheet is an accumulated figure.

Q. But it is the same figure in the income account, isn't it, for that year, because that is the first year you used it?

A. That is correct.

Q. So we are just at the same place where we split off?

A. As to 1942 we are.

Q. Yes, as to 1942. Now you come to 1943. Just indicate the page where I will find those deductions from your income account.

A. Find them on pages 16 and 17, accounts 270½ and 331½.

Q. Now, for 1943 in the account 270½—no, that is not the same thing, is it?

A. That is amortization of defense projects.

Q. That is not equipment?

A. Equipment is under 331½.

Q. All right. Now I have got it. Your equipment amortization of defense projects, $1,173,007.37, is deducted in arriving at your net income for the year?

A. It is.

Q. Is that all the deduction taken by way of amortization, obsolescence or depreciation of equipment?

A. No, shown in account 331 is normal depreciation.

Q. That is not charged to your normal depreciation?

A. That is correct, except that it is the same thing, because when we take amortization we don't take normal depreciation.

Q. On the same items. But you take normal depreciation on the others. Is that based on inspection?

A. It doesn't require inspection. We have certificates of necessity that authorize it under the section of the income [fol. 307] tax law over a period of sixty months or less if the war should end, for the purpose of income tax savings.

Q. But it is not an engineering amortizable figure?

A. That is correct.

Q. It just says you may take a certain percentage of items and amortize them as war instrumentalities?

A. That is correct.

Q. So that when this went in under that law you charged up against income this amortization factor which the law lets you do, but it represents no engineering fact; is that correct?

A. That is correct.

Q. All right. How about road structures?

A. Amortization there.

Q. Amortization there.

A. Amortization of road could involve property that is not depreciable as well as depreciable property.

Q. What account is that?

A. 270½.

Q. That is the one I lighted on first, wasn't it?

A. Yes.

Q. Well, what was the amount of amortization of road structure that was deducted in the year 1943? I have got it here. It is a trifling item, approximately $45,000.00.

A. Approximately $45,000.00.

Q. How about your account 268 where there is a deduction in this year for deferred maintenance of $1,586,577.00; is that correct?

A. That is correct.

Q. And that is in addition to your actual maintenance expenditures for that year?

A. That is correct.

Q. And that gives you some kind of a credit, does it not?

A. Sets up a reserve to take care of maintenance that was [fol. 308] not done in 1943.

Q. Have you set aside cash to take care of that reserve?

A. Cash or bonds, yes.

Q. And does that cash appear in your statement of cash on hand?

A. It does not.

Q. So that when you testified that you had certain cash on hand I think you stated it correctly there, that when you state your cash on hand, you leave out an amount of cash that is set aside to make this deferred maintenance reserve?

A. That is right.

Q. And did you state the amount of that cash?

A. I did.

Q. At the present time it is my understanding that exceeds $3,000,000.00. I just want to refresh my recollection.

A. It is in excess of $3,000,000.00, yes sir. I might say that some $400,000.00 of it has been expended this year, and the credit of that expenditure is reflected in the figures for 1944.

Q. You mean by that that $400,000.00 will not come in as an expense for the year 1944?

A. Not in our ICC or printed income accounts or reports to the Commission.

Q. So that in future years as you do maintenance and desire to charge some of it to this account—should I say charge or credit?

A. We charge that to the account.

Q. Charge some of it to that account, by that much you improve the earning picture for the year?

A. That is right.

Q. For the year 1943 under the law you deduct that reserve before computing your net income?

A. For ICC and other purposes, but not for income tax purposes.

Q. So if you have income taxes to pay you have to pay on [fol. 309] that?

A. That is definitely correct.

Q. And that has been included in your computations for income taxes for the year 1943?

A. Yes.

Q. You can make no charge other than for income tax purposes?

A. Not at the present time.

Q. And yet in the showing in your report as to the net income for the year 1943 there is $1,500,000.00 deducted and set aside in that reserve?

A. $3,500,000.00.

Q. For one year?

A. For the year 1943, yes sir.

Q. That is worse than I thought it was. I picked up a figure of $1,500,000.00 here in your——

A. You took the maintenance of way only.

Q. Oh yes, I took the maintenance of way.

A. Our figure includes equipment as well.

Q. And is there a cash reserve set aside for that equipment too?

A. There is.

Q. Not included in your cash on hand?

A. That is right.

Q. As I look now, Mr. Thompson, at your Exhibit 7 I see that for these first seven months of the year 1944 you have approximately $800,000.00 less gross revenue. Note I use the word "approximately."

A. The estimate was $956,000.00.

Q. Are you looking at No. 7?

A. Yes.

Q. I was looking at the month of July rather than the period of seven months. We will call it roughly $1,000,000.00 less income.

A. That is right.

Q. Now, you have got operating expenses have increased $4,817,736.72 or 21.63 per cent.

A. That is what the report shows.

Q. There is a large increase in 1944 in maintenance of way and structures of approximately $2,000,000.00.

[fol. 310] A. I will call it $1,900,000.00.

Q. And is that in addition to the $400,000.00 that has been charged to reserve?

A. That is in addition to the $273,000.00 charged to the maintenance of way part of the reserve.

Q. And the remainder of that $400,000.00 has been charged since this period?

A. Yes.

Q. Or when you used the figure of $400,000.00 did you include maintenance of way and equipment?

A. And maintenance of equipment.

Q. Now, I notice that the maintenance of equipment has increased by $1,703,000.00. I will agree with you and call it $1,704,000.00.

A. All right.

Q. Or 26.91 per cent.

A. That is correct.

Q. And that is in addition to what has been charged to maintenance of equipment reserve fund?

A. That is right.

Q. Is a large part of that additional expense there reflected in higher wages for employees?

A. Very substantial. The wage increase in effect today is approximately twenty-five per cent over the wages that are reflected in the figures of last July. That naturally picked up in November and December of 1943. We couldn't make them up in July. Therefore the comparable figure of last year includes a wage increase of approximately twenty-five per cent.

Q. Well, does that include payment for wages performed in 1943 that are paid in 1944?

A. There are no 1943 wage costs in 1944, that is, no substantial. Naturally we had to make an estimate for 1943, but we were within $50,000.00 or $60,000.00.

Q. Your transportation costs have gone up $953,000.00 plus?

A. That is right.

[fol. 311] Q. We will say $953,000.00. Is that largely due to wage increases?

A. Practically all of it.

Q. You gave us some figures as to the cash on hand on July 31st or August 31st.

A. June 30th was the last.

Q. June?

A. Yes, sir, that was the last published balance sheet.

Q. Was there one published at that time? Did you put it in evidence here?

A. Not today. It has been filed in court.

Q. Have you got more than one copy there?

A. I have the balance sheet. There is only one copy.

Q. Well, maybe we can get at it without my looking at it if I can find the balance sheet in here. Will you look at your last balance sheet? Now, what cash did you say you had on hand according to that balance sheet?

A. Actual cash is $6,570,000.00.

Q. And what temporary cash investments?

A. $11,005,000.00.

Q. What special deposits?

A. $2,900,000.00.

Q. Are those deposited and earmarked against something?

A. Special deposits are definitely earmarked.

Q. What are they earmarked for?

A. A lot of things.

Q. Well, now, let me put it another way to save you trouble. Any of those earmarked for your reserve fund?

A. No, sir, they are not. That is in a special account, "Maintenance Fund," not included in those figures I gave you.

Q. How about this general question: Was the $2,000,000.00 of special deposits earmarked to pay some of the current liabilities that are in your balance sheet?

A. Well, the biggest part of them on this balance sheet is the $2,700,000.00 of interest to be paid on July 10th, the [fol. 312] amount deposited with the various paying agents to pay the 1943 interest.

Q. That was the interest——

A. A big part of that $2,900,000.00 is that interest money.

Q. Well, on July 31, 1944, what were your total current assets?

A. They have not been published yet.

Q. Is it not on your report there?

A. June 30th.

Q. It would be much easier if you would say "Mr. Hodges, I have it for June 30th." I am not trying to trap you to get some information. Give it to me for June.

A. 33,285,000.00.

Q. And what are current liabilities?

A. $22,430,800.00.

Q. And the difference between your current liabilities and your current assets on that date are in substance different than the difference between your current liabilities and current assets on December 31, 1943?

A. They are very, very close together.

Q. Meantime you have paid out the Junction interest of about $2,700,000.00?

A. That is right.

Q. Now, have you some inside information as to how things stand today as distinguished from June 30th?

A. I do not.

Q. [illegible]w what your cash balance is today?

A. [illegible] sir.

Q. It is not as good as it was June 30th, is it?

A. No.

Q. Well, let's have it.

A. The balance as of August 28th $6,183,000.00.

Q. Have your temporary cash investments increased?

A. No, they have not.

Q. Any special deposits? As a matter of fact, they have [fol. 313] decreased?

A. The special deposits naturally decrease on the payment of interest.

Q. Unless you get some more. Have the trustees any special accounts or reserves in which the cash is deposited not included in these statements?

A. Other than definitely earmarked deposits, but they are all included in these statements.

Q. The three million and one-half reserve is not included in your cash statement?

A. That is correct. I have said that is a special account called "Maintenance Fund."

Q. Now, have you any other reserves where there is cash to take care of them that do not appear in your cash?

A. No other than earmarked for special things.

Q. That is what I want to know.

A. I can read into the record the detail of these special deposits if you wish. There are no others.

Q. It is not so much I want the detail, but I think I can frame a question that you can answer very easily without being trapped. You have here one reserve of $3,500,000.00, and you have set aside and earmarked some money to take care of it, and it doesn't show in your cash account?

A. That is correct.

Q. Is there another reserve where the cash has been set aside and it doesn't show in your cash account?

A. I don't know of any.

Q. Is there any other special account where there is cash that does not show in your cash account?

A. Not that I know of.

Mr. Hodges: Thank you. Mr. Thompson, I may want to call you back on some of these things after I have a [fol. 314] chance to look at these records and see if there is anything I want to verify.

Mr. Shafroth: If the Court please, we discovered this morning that we had neglected to file the answer of the Insurance Group Committee. It was discussed in New York in June, and a copy was supplied to Mr. Watts at that time. A copy of this answer—through inadvertence it was not filed. We ask permission to file it at this time.

T. A. Thompson resumed the stand for further

Cross-examination.

By Mr. Homire:

Q. Mr. Thompson, you referred to the tunnel accident that occurred last year. Will you state for the record what that accident was?

A. We had a fire and cave-in in tunnel No. 10 of the Moffat Tunnel road on the Denver & Salt Lake Railway which occurred on September 20th and was opened on December 1st, necessitating rerouting of all traffic by the Royal Gorge route.

Q. You have testified to a decline of the gross earnings of the railway, gross revenues, which is in comparison with the decline in the net rather slight. Can you give me the reasons in general for the great decline in net as compared with the rather smaller decline in gross?

A. Well, there is the increased charges to amortization, and the major cost, of course, being the increased cost for both labor and material.

Q. Have you made any studies or study as to the comparison of present unit costs of materials and supplies with any earlier period?

A. I made a study some two or three months ago; com- [fol. 315] paring with the costs of 1939.

Q. Comparing current unit costs with unit costs of 1939?

A. Yes, both labor and material.

Q. Will you state the result of your studies and percentages on both materials, supplies and labor?

A. That study showed an increase of approximately sixteen percent in the unit cost of materials and supplies, and an increase of between twenty-nine and thirty percent in the basic hourly rates for all labor.

Q. Have you any results of that study in terms of dollars that you could give us at this time?

A. I haven't. I could calculate it very easily from the information I have in my office.

Q. If we continue after lunch would you produce that at that time?

A. I will be glad to.

Q. What is the present annual accrual for roadway depreciation of the railroad?

A. Approximately $790,000.00.

Q. And does that include shop machinery that is used in the repair and maintenance of equipment?

A. It does.

Q. You testified that the Commission changed the accounting rules pertinent to depreciation of roadway and structures, making that depreciation mandatory instead of optional, and that that change took effect I believe January 1, 1942?

A. January 1, 1943.

Q. 1943. Will you state your understanding as to why the Commission made that change?

A. I presume because they thought it was sound accounting. The Commission has since 1925 had a docket of its own, endeavoring to set up depreciation on road accounts, and it has been discussed back and forth between the various railroads and the AAR, and finally in 1942 they issued [fol. 316] an order making it mandatory as of January 1, 1943. Prior to that time it was optional, and I believe utilized by very, very few railroads.

Q. And it would be presumably the purpose of sounder accounting practice for the purpose of reflecting more accurately the available income?

A. I think so.

By Mr. Gibson:

Q. You said accruals for roadway depreciation approximated $700,000.00. I was wondering if we could be slightly more exact. I notice on page 4 of the 1943 annual report to stockholders a statement that the accruals for roadway depreciation were $664,000.00 chargeable to maintenance of way and structures, and $112,000.00 to shop and power plant machinery which is charged to maintenance of equipment expenses. The total of those would be about $775,000.00 or $776,000.00. Would that be a more accurate figure?

A. That would be a more accurate figure.

Mr. Homire: Thank you.

By Mr. Hodges:

Q. Mr. Thompson, you have given your opinion on this accounting question in the deduction of depreciation on road and structures. You know that the railroads resisted it for a great many years?

A. I do that.

Q. And did you know the legal reasons for resisting it?

A. Not without going back and looking them up.

Q. You didn't take into consideration in giving your opinion the rulings of the Supreme Court of the United States on the question of depreciation?

A. I did not.

Q. You know that this depreciation is not based on inspection?

A. That is right.

[fol. 317] Q. And you know that the attitude of the railroads over all these years has been that there is no such depreciation?

A. I am familiar with that.

Q. And that for all these years the Interstate Commerce Commission has merely said to you "Well, take it if you want to"?

A. That is correct.

Q. And now they have made a ruling, and do you have any information on whether that ruling is good as against the law as declared by the Supreme Court?

A. Not from a legal standpoint.

Q. Now, you said that there is an increase over 1939 of sixteen per cent in material cost?

A. That is right.

Q. How wide a field do you cover in that material?

A. Approximately ninety per cent of all material used.

Q. Rails?

A. Rails.

Q. Ties?

A. Ties, coal.

Q. Everything that goes into the construction of a railroad?

A. Maintenance in particular.

Q. Maintenance is really keeping up the constructive plan, isn't it?

A. Yes sir.

Q. You say that is sixteen per cent?

A. Sixteen per cent, yes sir.

Q. And you say that the labor costs have gone up about 29%?

A. That is right, twenty-nine to thirty per cent.

Q. That is not your own opinion, is it?

A. Well, for the record I will state that I made a very careful study and comparison of the present day costs with 1939 costs. The wage rates are a matter of record in the reports of the Commission. I used those reports, and, incidentally, thirty days after I made that report the Interstate [fol. 318] Commerce Commission made a study for the railroads of the United States and quoted the identical figure on wage rates in the nation-wide area.

Q. Well, so far, then, as material and unit costs enter into the estimate of the reproduction cost of the railroad, you would have to increase your material costs by about sixteen per cent and your wage costs by twenty-nine to thirty per cent compared with estimates made in 1939?

Mr. Gibson: I think that is purely a legal question. Any gentleman can answer that quite as effectively by briefs as they can by the witness on the stand.

The Court: I wouldn't ask anything about a Supreme Court decision. I would just ask him what his figures show.

Mr. Hodges: It is not asking what the Court said. Before I did ask him that, and he so testified, because he gave an opinion as to a certain account, and I didn't object to it. This is a factual thing.

Q. (Question read to the witness.)

A. Yes.

By Mr. Gibson:

Q. But even after doing that, you wouldn't earn any more, would you?

A. No.

The Court: Is that all of this witness, gentlemen? Step down.

Mr. Keegan: If the Court please, the City Bank Farmers Trust Company has about three more exhibits here. We probably will have——

Mr. Gibson: May it be understood that this forthcoming evidence will be applicable to all the issues raised herein?

[fol. 319] The Court: Yes.

Mr. Keegan: We have an exhibit here marked 9 and they want another letter to go with it. I would like to reserve that until after lunch, and go ahead with the exhibits that have been marked for identification as Nos. 10 and 11. If the Court please, in explanation of our Exhibit No. 10 you will recall that Mr. Thompson on our direct examination stated that if we wanted to compute the debtor's income available for interest so as to include the Reconstruction Finance Corporation's interest and the Chase National Bank loan interest you would take columns 2, 4 and 6 in the top block of figures on page 32 of the 1943 annual report, Exhibit No. 8, and add those three columns together. That is what we have done on the computation for column II of

Exhibit 10. Mr. Thompson stated that would be the way to make it. In the third column of Exhibit 10 under the heading "Debtor's Interest Requirements for Securities Senior to General Mortgage Bonds including Interest on Unfunded Debt," there again we have simply made the computation which Mr. Thompson said should be made, namely, adding the total interest on the funded debt as shown in column 1 of the second block of figures on page 32, and added to it the RFC and the Chase National Bank loan interest and then deducted the $1,494,400.00 interest on the General Mortgage bonds in order to get the senior interest ahead of us. Then, the last column IV of Exhibit 10 is simply the difference between columns II and III. It shows each year whether the debtor's income available for interest was more or less than enough to take care of the interest on senior debts ahead of us. The summaries are given and the only one that is estimated—the only figure that is estimated is [fol. 320] the income for the balance of 1944. We have the exact figures for the first seven months, and we have estimated that it would keep up at that same ratio, which I think is ultraconservative, and we figured the entire income of 1944 on that ratio. I had these figures added and subtractions made by our bookkeeper and checked by our office auditor, and then I checked the adding machine tape, and to the best of my knowledge they are accurate.

Exhibit No. 11 simply starts out with the first plan of reorganization which was submitted, which was the debtor's plan back in 1936; shows what the proposal was; how much stock in the reorganized company it was supposed to give the General Mortgage bonds at that time; what the current earnings were at the time that plan came out, and what the accumulated earnings over senior interest to last December 31st were at that time. We have given in a footnote there a reference to the printed record where all of those plans can be found, and the amounts in column III as to what the proposal was to give the General Mortgage bonds in each plan throughout the years, that was taken from the part of the record indicated in the footnote. Then we come to column IV to find out what the current earnings were for that particular year when that plan was proposed. Those figures are simply transposed from our Exhibit 10, and the accumulated surplus is also transposed from our Exhibit 10. It is just a matter of running them off on the adding ma-

chine. I would like to offer at this time our City Bank Farmers Trust Company's Exhibits Nos. 10 and 11.

The Court: Is there any objection? If not, they will be admitted.

Mr. Homire: Is there to be no witness introduced to support these?

[fol. 321] Mr. Keegan: I am perfectly willing to swear, if you think it is necessary, that these computations—we had Mr. Thompson testify how the computations should be made. The question of computations was just running them off on the adding machine and making the necessary additions and subtractions.

Mr. Homire: I would just like to ask you one or two questions. In the exhibit that shows the various balances made on various plans, what number is that?

Mr. Keegan: That is No. 11.

Mr. Homire: Of course, the capitalizations that are subjected to your analysis here in the various plans were not always the same in the various plans: is that not true?

Mr. Keegan: That is correct. You mean, for instance, the debtor's plan in 1936 would have one capitalization, and the Insurance Group plan No. 1 would have another capitalization?

Mr. Homire: Yes.

Mr. Keegan: That is right.

Mr. Homire: So the capitalizations vary, and taking a percentage of allotment to the General Mortgage under one capitalization would not necessarily be an exact or intelligible comparison with another percentage under another capitalization. That necessarily follows from the fact that the capitalization was different.

Mr. Keegan: I would suggest you put in the capitalization, and you can draw your own conclusions. We had that as an exhibit in one of our briefs.

Mr. Homire: I don't think it is necessary so long as you say the capitalization under the different plans is different. [fol. 322] Mr. Keegan: This is not a per cent of the capitalization. For instance, take line 1 of Exhibit 11, and under III we note the debtor's original plan or proposal was to give the General Mortgage bonds new stock equal in par value to 100 per cent of their claim, and so on down the line.

Mr. Homire: But you are giving them fractions of the different capitalizations in the different cases you compared.

Mr. Keegan: The capitalizations vary. I will be glad to give you the proposed capitalizations if you think that will help.

Mr. Homire: I don't think it is necessary. I just wanted to bring out the point the capitalizations were different. The only other objection is that during the progress of the proceedings the senior debt was increasing on account of the accumulated unpaid interest. That also is a fact, is it not?

Mr. Keegan: That is a fact. That is shown graphically on this Exhibit No. 10. It shows it year by year down to the date of the plan.

Mr. Hodges: I should like to put in a caveat to that statement.

Mr. Gibson: Will you let me ask a question or two for information there?

Mr. Keegan: Certainly.

Mr. Gibson: Is the purpose of these statements to support a request by the General Mortgage bondholders for a payment of cash to the General Mortgage bondholders, or for some increase of securities to the General Mortgage [fol. 323] bondholders?

Mr. Watts: May I answer that question? Mr. Keegan prepared these exhibits at the request of the General Mortgage Trustee and its New York counsel. They are to be used just incidentally in connection with Mr. Keegan's question of the possible redistribution of the bonds of the reorganized debtor which were released through the purchase of the Junction bonds, but primarily and principally they are to be used in connection with the question of the reasonableness of the action of the General Mortgage bondholders in voting to reject the plan by a vote of 79.33 per cent. It is evidence of the facts that in a general way were before those bondholders at the time each of the various proposals were put forward, and what the general situation was at the time they voted on the plan.

Mr. Gibson: In translating that to the terms of Mr. Keegan, I understand that these statements are introduced for the purpose of supporting a claim for an increased allocation of new securities to the General Mort-

gage bondholders, and not in support of a payment of cash for the general bonds. Is that correct?

Mr. Watts: No, it is not quite correct. They are not introduced for the purpose of supporting any increased securities or payment of cash, but merely on the question of the reasonableness of the vote.

The Court: Is the reasonableness of the vote on any class of securities an issue in the case?

Mr. Watts: A very important issue.

The Court: Is that in question, the reasonableness——

Mr. Watts: Yes sir. We didn't intend to come to [fol. 324] that until later.

The Court: You are referring to Exhibit——

Mr. Watts: It says in Section 77 (e) if the plan has not been accepted by the creditors and stockholders, that is, if it has not received a two-thirds vote by each of the classes entitled to vote, and that is the case here, the judge may nevertheless confirm the plan if he is satisfied and finds after hearing that it makes adequate provision for fair and equitable treatment for the interests and claims of those rejecting it. And here is the point: "that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts." And then it continues by requiring the Court to find again that it "conforms to the requirements of classes (1) to (3) of the first paragraph of this subsection." We think it is of great importance that the Court must find after hearing that the objection was not reasonably justified, and we believe these exhibits throw a great deal of light on that question of whether the objection was reasonably justified.

Mr. Gibson: I understand that these exhibits are not introduced for any additional payment on the General Mortgage bonds.

Mr. Watts: This is right.

Mr. Gibson: Mr. Keegan, I notice in column III the interest on senior indebtedness is computed according to the expressed interest rate of collateral notes, without recognizing the interest on the collateral. Is that right?

Mr. Keegan: Yes, it is my understanding that on page 32 of the last annual report that that Reconstruction Finance Corporation interest is the interest on that collateral.

[fol. 325] Mr. Gibson: And simultaneously for the Chase National?

Mr. Keegan: Yes. We simply add those columns together and subtract the interest on the General Mortgage.

Mr. Gibson: Am I correct, then, in understanding from your Exhibit 10 that interest requirements on the senior debt, even when computed in the method you followed, were not covered? There was a failure to cover them by over $16,000,000.00 from the inception of the reorganization proceedings down to the year of 1942, and it was only by including the surplus of the four years that the correct amount was computed; is that a correct statement?

Mr. Keegan: I think that would be a substantially correct statement.

Mr. Watts: That is not surplus cash. It is a statement of the earnings available.

Mr. Gibson: Thank you for giving me a better impression.

The Court: May I ask you a question, Mr. Keegan?

Mr. Keegan: Yes sir.

The Court: In the third supplemental report, which is the plan for the consolidation of the Salt Lake, the Rio Grande Junction bonds are allowed $2,121,000.00 first mortgage bonds and $634,000.00 of income bonds. Do you want those particular securities reallocated to the General Mortgage bonds? What securities do you want? Do you want a block of common stock?

Mr. Keegan: We intended to cover that in detail in our argument. The way that will work out is this. In our [fol. 326] argument we want to review some late decisions of some other railroad reorganizations where surplus cash was used to reduce senior claims and the courts have required that proper adjustments be made as we have asked here. When the Commission promulgated the plan two and three-quarter million dollars of Junction bonds were outstanding to the public, and they naturally figured they would have to use the new bonds in place of them. Now that the trustees have purchased them and the bonds have been taken out of circulation our position is that by reason of their having purchased those bonds, it is no longer necessary to issue new bonds in exchange for them. Consequently that releases two and three-quarter millions of securities in the new company for redistribution generally. The way that works out is a matter of railroad accounting. The Commission has already fixed the relative position of the parties. The way these cases I intend to review in my

argument have handled that, they just made a general distribution of those on the same basis as the original distribution, and the way it works is that we get better treatment; everybody gets better treatment. For instance, in this appendix here the First Trust 4s are originally getting seventy-three per cent in new first mortgage bonds and twenty-eight per cent in new income bonds. They will get a little higher ratio in the distribution of the new first mortgage bonds and less of the new income bonds, and on down the line everybody's treatment will be sweetened a little, and when the ones next ahead of us are sweetened they are getting less common stock and better securities, so it releases $2,758,333.00 of par value common stock at the end which becomes available for the General Mortgage bondholders.

[fol. 327] The Court: Aren't you violating the priority rule as set out in the Milwaukee case? That is a question of argument, though.

Mr. Keegan: If you want me to go into those cases to show how those courts have been doing that— They had their hearings since last fall. There have been several cases come down where they have done this very thing, and I would like to discuss that in detail and show how that works out.

The Court: Well, we will not do that now. Put your evidence in.

Mr. Keegan: I offer these two exhibits.

The Court: They have been admitted.

Mr. Keegan: That is all the evidence we have at this time, although, as I understand it, what we are doing now is trying to segregate this Junction issue. After lunch it will take about twenty minutes to argue that. We do have some broader objections, and Mr. Watts would like to have the right to interpose some evidence later on our broader objections.

The Court: Do you want to introduce that before the argument?

Mr. Keegan: Whatever you prefer.

The Court: Let's have all the evidence first.

Mr. Watts: Your Honor please, I should like to call Mr. Miles C. Kennedy.

MILES C. KENNEDY, a witness called and sworn on behalf of the City Bank Farmers Trust Company, testified as follows:

[fol. 328] Direct examination.

By Mr. Watts:

Q. Mr. Kennedy, will you give your name and address?

A. My name is Miles C. Kennedy. I live at 45 Fifth Avenue, New York.

Q. What is your profession, Mr. Kennedy?

A. I am a consulting engineer. I am a member of the firm of Coverdale & Colpitts', consulting engineers, office at 120 Wall Street, New York City.

Q. Will you please give a brief statement of your professional experience?

The Court: Is there any question as to his qualifications by anyone?

Mr. Homire: We will waive any question as to that.

Mr. Gibson: We will do likewise.

The Court: All right.

Mr. Watts: Your Honor, may I inquire whether that goes to the extent of—I hope to bring out in these qualification questions the fact that the witness and his firm have in a very large number of railroad reorganizations served as special advisers and consultants to the bondholders, bondholder committees, creditor groups and the like.

The Court: That fact is well known to the Court and I presume it is to all the parties here.

Mr. Gibson: We so admit.

Q. Mr. Kennedy, I am about to lay the groundwork for rather an important question for the General Mortgage Trustee. I will ask you whether you have examined at our request the two exhibits which have just been introduced, being City Bank Farmers Trust Company Exhibit 10 and [fol. 329] Exhibit 11, the first of which is entitled "Table Showing Debtor's Income Available For Interest And Interest Requirements For All Securities Senior To General Mortgage Bonds For Each Year During Reorganization Proceedings," and the second of which is entitled "Table Showing (a) Current Debtor's Income Available For Interest And (b) Surplus (Or Deficit) Of Total Debtor's Income Available For Interest To Last Previous December

31 Over Interest Requirements To The Same Date Of All Securities Senior To General Mortgage Bonds (Including Interest On Unfunded Debt), All As Of The Respective Dates On Which The Several Plans Were Proposed—As Well As The Treatment Proposed For General Mortgage Bonds In The Several Plans"?

A. I have.

Q. To the best of your knowledge, Mr. Kennedy, has the substance of the information which is outlined in both of these tables, and particularly the table included in Exhibit No. 11, been available to the public and to the holders of the General Mortgage bonds?

A. Yes, it has. Perhaps not in exactly this form, but it could have been arrived at by very simple computations. The income accounts are, of course, published in the daily press, and all the information in regard to the plan has been in financial papers, dailies, weekly, statistical services and the manuals which are readily available.

Q. Mr. Kennedy, in your opinion is this the kind of information which would and which should be carefully considered by the General Mortgage bondholders in determining how they should vote on the acceptance or rejection of the plan of reorganization?

A. Yes, I think it is very important information. All the relevant facts are important, of course, and these do not purport to be all the relevant facts.

Q. Mr. Kennedy, will you explain in a little more detail what you conceive to be the particular significance of Ex- [fol. 330] hibit No. 11 or the figures which are set forth in the table on Exhibit No. 11?

A. Well, I think one of the highly significant facts set forth in Exhibit No. 11 is the sum total of the accumulated surplus table arrived at in column V in line No. 12 which shows that as of December 31, 1943, the last previous year end to the submission of the plan, all the interest on obligations senior to the General Mortgage bonds had been earned with a margin of $3,859,306.00 to spare. In other words, if the amounts earned available for interest on the senior obligations had been paid to the holders of those obligations, the position of the General Mortgage would have been no worse than it was at the beginning of the receivership. Now, as compared to that, the other significant fact is shown in the percentages on column III of this exhibit, which shows that in the first plan filed, which was the debt-

or's plan, the General Mortgage was accorded 100 per cent treatment in new preferred stock, that is, preferred stock in the proposed new company. That is, they would have gotten dollar for dollar in par amount in satisfaction of their claim as of that date, of their principal amount as of that date. The next plan was the Insurance Group plan of 1937 which gave the General Mortgage 100 per cent in new common stock. After hearings before an examiner of the Interstate Commerce Commission the examiner recommended fifty per cent in new common stock. The Interstate Commerce Commission in two subsequent plans awarded thirty-three and one-third per cent. One of these was in 1939, and one was in 1940. A certain discussion plan more or less agreed upon—I don't know exactly—in 1941 again gave the General Mortgage bonds fifty per cent. The Court's [fol. 331] plan of 1941 brought the amount to 32.99 per cent, to practically thirty-three per cent, and in 1941, skipping down to line 9, the Insurance Group plan accorded the General Mortgage 47.42 per cent. Then we get along to 1942 and the Interstate Commerce Commission cut the percentage down to five per cent, and in 1943 they doubled that treatment by giving them ten per cent. Now, coupled with that fact is that the earnings of the property had been improving steadily since about 1937, when, according to Exhibit 10, there was a deficit of $249,880.00 in income available for interest. Those earnings increased very substantially, due in part I should say to the generally increasing prosperity, due in rather large part I should say to the improvements which were being made in the debtor's program, under which very large amounts were spent for improvements which it is reasonable to assume produced very substantial savings or increases in revenues.

Q. It is true, is it not, that the figure $3,859,306.00, which you referred to as the figure in column V, line 12, that is, $3,859,306.00, represented the accumulated surplus up to December 31, 1943, of the income available for interest over the interest requirements of the so-called senior obligations? It is true that the period during which that figure was built up included some abnormally good years; is that not so?

By the Court:

Q. It included war years?

A. Yes, up through 1943. Obviously those were abnormally good years, but it may also be said that some of these

years were abnormally bad years, and, furthermore, in some of these years in the period, perhaps all of them, the earnings were reduced because of the expenses incident to the very large improvement program which I just men-
[fol. 332] tioned.

By Mr. Watts:

Q. Mr. Kennedy, in referring to what might be called the deterioration in the treatment for the General Mortgage bondholders as outlined in column III of Exhibit 11, you are, of course, familiar with the fact that the total capitalization provided for in the several plans was not uniform; there were some changes?

A. Yes, I am aware of that.

Q. And although the figures do not appear in this exhibit, if I advised you that, for example, in the first Insurance Group plan, which is the one referred to in line 2 of that exhibit, the common stock which the General Mortgage bondholders were to receive constituted 100 per cent of the common stock provided for in that plan, and that in each of the subsequent plans through the Insurance Group plan No. 2 which is referred to in the ninth line of that exhibit, all of the allotments of the common stock in the various plans to the General Mortgage bondholders constituted a minimum of approximately thirty-three per cent of the total amount of common stock in the reorganized company to be issued under the plan; would that factor be of any significance to you in your answer to that question?

A. Will you let me see those figures?

Q. Yes, they are set forth in the last column on page 6 of the brief which we filed with the court last September, a year ago.

A. Well, these figures show that not only did the General Mortgage bonds get less per dollar in new stock, but that they got increasingly smaller portions of the common stock to be issued.

Q. So in a general way that fact merely increases the
[fol. 333] change or tendency shown by the other features of the plan?

A. Yes, it does.

Q. Now, Mr. Kennedy, you know, I believe, that in view of the fact that the interest on the obligations prior to the General Mortgage bonds was, taking this period up to December 31, 1943, as a whole—in spite of the fact that that

interest was earned, no interest was paid until sometime after December 31, 1943?

A. Yes, that is my understanding.

Q. Do you know what was done with the money which was earned but which was not paid out to the security holders?

A. Yes, I do in a general way. Up to the end of 1943 the trustees under the direction of the Court had expended, I think, about $37,000,000.00 in improvements, additions and betterments to the property. All of that money did not come from the accumulated earnings set forth here. Part of it came from equipment trust issues I think in the amount of some five to six million dollars. Part of it was, of course, accrued in depreciation accounting, but it is quite clear that the earnings of the property throughout this period in general have been used to improve and strengthen the property in the discretion and wisdom of the trustees and the Court.

Q. And in addition, of course, you are familiar with the fact that over the period as a whole there has been an increase in the cash and current assets over current liabilities?

A. There have been very substantial increases.

By the Court:

Q. Take that column III, Exhibit 11, which shows the amount of common stock, are those percentages, fifty per cent, 100 per cent, of the same amount of common stock?

A. No, sir, they are not percentages of an amount of com- [fol. 334] mon stock at all. They are percentages of the dollar amount of the new stock at par which is given to each $1,000.00 bond.

Q. The minimum is thirty-three per cent, and then again we have next thirty-three per cent. Thirty-three per cent of the larger amount of common stock?

A. No, I don't believe it is a larger amount, but I believe it is of a smaller amount. The figures on the exhibit, line No. 2, for instance, the Insurance Group plan of 1937 where it says 100 per cent in column III that means for every $1,000.00 of General Mortgage claims there would be distributed $1,000.00 of new common stock, that is, dollar for dollar. In line 3 where it says fifty per cent, it means that each $1,000.00 of claim would get $500.00 in par amount of new common stock.

Q. It has no relation to the total amount of the issue of common stock, has it?

A. No, but I can give you that figure if you care to have it.

Q. I just wanted to know if those figures were fifty per cent of the amount of common stock.

A. The result of these various treatments was that the proportion of the total issue of new common stock to be received by the General Mortgage became increasingly less as time went on.

Q. Take the last two there, 5% and 10%, it might be 5% of a lesser amount of total common stock, and it might be 10% of a larger amount?

A. Well, I can tell you exactly what that is. Five per cent would also have been five per cent of the new common stock. Ten per cent treatment would have amounted to twelve per cent of the new common stock.

By Mr. Watts:

Q. In other words, when the 1943 plan came out there was a slightly smaller amount of common stock authorized? [fol. 335] A. That is correct, and therefore ten per cent made a larger amount of the total.

Thereupon a recess was taken until two o'clock p. m.

Pursuant to recess the following proceedings were had at two o'clock p. m.:

MILES C. KENNEDY resumed the stand for further

Direct examination.

By Mr. Watts:

Q. Mr. Kennedy, in answer to one of my recent questions you were explaining some of the significant features of Exhibit No. 11. Now, Mr. Kennedy, assuming the correctness of your conclusion that funds were diverted from the payment of interest on secured obligations for the purpose of making large improvements in the property intrusted to the debtor's trustees, what conclusion would you or a General Mortgage bondholder be warranted in drawing from that fact?

The Court: You want him to put himself in the position of a bondholder?

Mr. Watts: Yes, your Honor.

The Court: Well, has he the right to do that? He may state what facts were before a bondholder, but what conclusion the bondholder would draw from them he can't state, can he?

Mr. Watts: Well, sir, the way I feel about it is this: that we are speaking about what would be reasonable conduct for a holder of General Mortgage bonds, and we believe that the views that Mr. Kennedy would have in the light of [fol. 336] his experience, and with his access to what is a matter of public information on this issue would be very similar to the—the conclusions he would draw would be very similar to the conclusions any normal similar person would draw. May I change it and ask Mr. Kennedy what conclusions he would draw from that fact?

Mr. Homire: If he were a bondholder?

Mr. Watts: No, just from those facts what conclusion does he draw?

A. Well, I would start out with the assumption, I believe, that the trustees of this property were acting with all wisdom and discretion not only because they were appointed by this Court and confirmed by the Interstate Commerce Commission, but because I know and I believe it is a matter of general information that the trustees have done an outstanding piece of work for this property. I would therefore believe that in diverting funds from the payment of interest to investments in the property the trustees were doing what they believed and what was for the benefit of the debtor's estate and for the security holders for whom they were trustees. From that I draw the conclusion that they considered the investment of this money in additions and improvements much more beneficial to the security holders of the company than the payment to them of current interest, because I do not believe that they would do anything to worsen the position of their security holders or any class of them; certainly not willingly. Now, of course, it is reasonable to believe that the expenditures that these trustees made have been productive and will be productive of very substantial earnings. I spent several years with the Pennsylvania Railroad making economic studies of the [fol. 337] savings it had out of new work, the added traffic

to be obtained by new lines and extension of lines, and I know very well an improvement that didn't earn fifteen per cent on its cost or was not estimated to earn fifteen per cent on its cost would receive no consideration whatever from the management, and I therefore assume that these improvements or most of them could be expected to earn ten per cent to fifteen per cent or even more in some cases. Now, if that is the case the position of the bondholders is improved, and even though money has in effect been borrowed from the bondholders through the non-payment of interest, which has been used for making improvements, there is bound to be considerable income in excess of the interest that will be paid on that money when interest is again resumed, and that benefit would flow down to the junior issues in the reorganization. I should therefore conclude that the position of the General Mortgage—what I have already said is true—the position of the General Mortgage should be better rather than worse through the expenditure of this money by the trustees even though it has meant the piling of additional debt ahead of the mortgage.

By the Court:

Q. Assuming that this expenditure is proper, would it not be better today not to pay the interest and make the improvements than to go out and borrow money to make the improvements?

A. Of course, I take the position you are borrowing the money anyway which has been earned by your bonds, and you are retaining it and not paying it out to them——

Q. Are they entitled to the earnings of the road until the road is properly maintained; all of the earnings except [fol. 338] those necessary for the maintenance of the property?

A. I am not talking about maintenance. I am talking about improvements over and above the maintenance.

Q. What improvements were not necessary in order for the company to earn income?

A. You could have replaced various parts of the property in kind. Instead of that you went out and built better bridges than you had before. You bought better equipment than you had before. Understand I am not criticising in any way any part of this program. Relying upon the trustees, as I said, I have no inclination to criticise anything that was done. I am saying, however, that the

money that was used to make a substantial part of these improvements was in effect borrowed from the bondholders and claims piling upon the reorganization on which interest will be paid.

Q. How were they denied this money if there wasn't money enough to make improvements and also pay interest? Are the bondholders entitled to these earnings at the expense of the maintenance of the property?

A. I wouldn't give them credit for one cent over the earnings of the property, but I draw a sharp distinction between the earnings of the property and the maintenance because the ICC makes a distinction in them.

Q. What on this property are the improvements? Don't you think it is better to put in the heavier rail in order to carry on its work and do a good job?

A. Yes sir, I do.

Q. And if it hadn't done a good job they would not have been earning anything at all? They would have been sunk as they were before the reorganization.

[fol. 339] A. That is quite possible. I think the earnings of the property have undoubtedly improved because of this program, but nevertheless the records show that very substantial amounts were spent for additions and betterments which were over ordinary maintenance, and it is my view, whether I am correct or not, that the bondholders, unless they acquiesced in that move, would have had the right to come in and protest against the expenditure of this money for improvements as against paying interest on their bonds.

Q. Is there any law supporting that position, do you know?

A. I don't know, sir.

Mr. Hodges: I can cite you a case in the Third Circuit Court of Appeals. I will give it to you.

The Court: Very well.

By Mr. Watts:

Q. Mr. Kennedy, you spoke before of a substantial improvement in the debtor's cash position as of December 31, 1943. Can you tell me what the cash position was on that date? I believe that is in the report of the trustees.

A. I have it here somewhere. If you will give me that 1943 report that Mr. Thompson introduced——

Q. Yes (handing document to witness).

A. From page 12 of this Exhibit No. 8 which Mr. Thompson introduced this morning, the cash as of December 31, 1943, was $12,716,924.00. Temporary cash investments were $8,005,000.00. Total current assets were $33,915.00, roughly, and current liabilities were $23,517,000.00, also roughly, which gives net working capital of approximately $10,400,000.00.

Q. Were there also shown special deposits aggregating a [fol. 340] little over $609,000.00?

A. That is true, but I haven't mentioned them because Mr. Thompson brought out this morning they were definitely earmarked for special purposes.

Q. Mr. Kennedy, in view of the cash distributions which have been and were being provided for security holders in numerous other reorganization proceedings before the Interstate Commerce Commission and before the courts, was it in your opinion reasonable for the General Mortgage bondholders to assume that some of this cash to which we have just been referring might be used to reduce accrued interest on obligations prior to the General Mortgage bonds, and thus improve the position which the General Mortgage bondholders might expect in the plan of reorganization?

A. Yes, I think so. I can think of several cases where cash distributions were made to reduce claims, and those cases, generally speaking, received rather wide publicity, and it would be quite natural for bondholders not only in this company but in other companies to expect or have strong hopes that similar distributions would be made in these cases.

Q. I come now, Mr. Kennedy, to the question for which I have been laying the groundwork by these previous questions, and first I want to read again certain language of subsection (e) of Section 77 of the Bankruptcy Act, which says that; "if the plan has not been so accepted by the creditors and stockholders"—that means by the vote of two-thirds of each class of securities entitled to vote—"the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing,"—then I will skip a little—"that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the [fol. 341] relevant facts." Without reading the balance of these requirements, in your opinion, based upon your general experience in such matters and upon the testimony which you have just given, was the rejection of this plan by

the General Mortgage bondholders reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts?

Mr. Gibson: Your Honor please, that forces an ultimate question of law. The statute implies whether your Honor is satisfied, not whether Mr. Kennedy is satisfied. We doubt if the witness is competent to express an opinion on that ultimately.

The Court: I think the objection is good, but I will let him answer if you want it in the record.

Mr. Watts: We are just asking his opinion.

The Court: You are asking his opinion how someone else should make up their minds. He can answer, but I don't know what value it will have.

A. In my opinion it was.

Q. Mr. Kennedy, I have here a five page pamphlet which is entitled in black letters "H. R. 2857," and in smaller type "78th Congress 1st Session." It appears to be a copy of a bill which was introduced in the House of Representatives on June 3, 1943, by Mr. Hobbs, and to have as its purpose the amendment of Section 77 of the Bankruptcy Act. According to the heading it was referred to the Committee on the Judiciary. Will you examine that (handing document to witness).

A. Do you want to ask me a question about it?

Q. Are you familiar in a general way with the text of that [fol. 342] bill?

A. Yes.

(Thereupon a document was marked for identification City Bank Farmers Trust Company Exhibit 12.)

Q. Mr. Kennedy, on the first page of that bill, beginning on line 8, will you read beginning line 8 of page 1 through the tenth line of page 2?

Mr. Homire: Your Honor, we object to any reference to this bill in the record. This is a bill which has been postponed and has not even been passed by either house of Congress, has no relevancy whatever to this case, and we object in the proceedings here.

Mr. Gibson: I think it is hard enough to operate under Section 77, much less something that has not been passed.

Mr. Watts: We are attempting to show here whether the action of the General Mortgage bondholders by voting by a vote of about four to one of those voting to reject the plan was something reasonable, whether it was reasonably justified in the light of all the relevant facts. This bill and the subsequent versions of it and the report of the Committee on the Judiciary, which was a unanimous report and which I want to offer later, was a matter which was widely publicized in the daily press. They are matters of which the bondholders may be expected to have had general knowledge. It would have had a great deal of effect on what their rights would be under a plan of reorganization, and I believe it has a very great bearing on the question of the reasonableness of their vote.

[fol. 343] Mr. Gibson: It may be natural and human to hope that something will turn up, but it can hardly be reasonable to rely on a bill which is so obviously doomed to rejection as this bill is.

The Court: The Court will take judicial notice that this bill has not been passed, and when offered there was a strong reaction against it. I would also want to get the advice there of the bondholders or the trustees or anyone else who was interested in it.

Mr. Watts: We propose to ask that ourselves.

The Court: I think I will sustain the objection. You may use it in your argument if you wish.

Mr. Hodges: May I suggest to your Honor that it is something of which your Honor can take judicial notice. There is a unanimous report of the House Judiciary Committee, giving its views on the meaning of Section 77 as it was originally passed.

Q. Mr. Kennedy, you are also familiar with subsequent versions of this bill which were variously referred to, H. R. 4873 of the 2nd Session of the 78th Congress, H. R. 4904 of the 2nd Session and H. R. 4960 of the 2nd Session?

A. That is correct.

Q. And from your general familiarity with the texts of these four bills do you know whether they related to substantially the same subject matter?

A. Yes, the substance is about the same.

Q. Are you also familiar with a twelve page pamphlet which I am now handing you, which is entitled "House of Representatives Report No. 1615, 78th Congress, 2d Ses-

sion,'' and which appears to be a report from the Com-
[fol. 344] mittee on the Judiciary, stating that H. R. 4960 as amended, having been considered, is reported favorably to the House with the recommendation that it do pass? Are you familiar with this report?

A. Yes, I am.

Q. And with the fact that it is stated in the report that it is unanimous?

A. Yes.

Mr. Watts: Your Honor, I suppose that this report would be subject to the same objection.

Mr. Gibson: We make the same objection.

Mr. Watts: I would like, however, for the purpose of the record to offer it and have it marked as City Bank Farmers Trust Company Exhibit 13 for identification.

The Court: Well, I have just found an extract here from a Los Angeles case where the Supreme Court said "The question of whether a plan of reorganization is fair and equitable is one of law, and the fact that the great amount of security holders vote against it is not the test. A plan can be approved by the Court that is fair and equitable even though the record number of security holders object." I suppose the opposite of that is true. You are arguing here that your client did not approve of this plan; that it disapproved of it.

Mr. Watts: Now we come to the question of whether the Court should confirm the plan over their objections, and that is quite a different question than whether the plan is fair and equitable. I am not offering this testimony on the question of whether the plan is fair and equitable. We [fol. 345] are offering this testimony on the question of whether the action of the General Mortgage bondholders in voting against the plan was reasonable in the light of the situation as it existed on that day; that is, in the light of all the information they had, whether on the basis of that they were reasonably justified in so voting.

The Court: You haven't offered any testimony that the security holders you mention knew of the Hobbs bill or it was called to their attention, or that they were influenced by it.

Mr. Watts: Well, sir, I propose to come to that. I am going to cover that in my questions to a later witness. I have here a man who has been consulted by a great many

of them, who has had to meet their inquiries and their complaints, and who knows from the telephone calls, from the letters he has received, that, generally speaking, holders of General Mortgage bonds of this road did know it.

The Court: The Court will take judicial notice of the fact that every stockholder who thinks he has been gyped thinks the Court has taken some action.

Mr. Watts: I think we are narrowed down to the question of whether our bondholders were reasonably justified in their vote, which is quite a bit different from whether this bill will become law or whether it should become law, or whether, it pending, it was reasonable for the bondholders to vote against it.

The Court: According to this Los Angeles case the Court shouldn't be influenced by it.

[fol. 346] Mr. Watts: That is on the reasonableness of the plan.

The Court: It is a distinction without a difference.

Mr. Watts: If there were no distinction it would not be necessary to provide for this second hearing on the vote. As we see it, first this matter came up on the question of reasonableness of the plan. Now, the Court has the right to decide on the reasonableness of the rejection. In the previous hearing we said the General Mortgage bondholders did not believe the plan was fair and reasonable. We argued this orally and we argued this in our brief. This Court decided differently. We believe it was proper for this Court to decide either way. It was a question on which reasonable men might differ, but when you get to this next question of whether this Court may confirm the plan over the objection of a great majority of one class of bondholders, we have something that is entirely different. Now, this Court under the statute must review the action it took last year, and, after hearing, it must again find that the plan was fair and reasonable. That is the first part of this provision. After it has done that, the Court must say "Well, then, I not only find that the plan is fair and reasonable but that you are not reasonably justified in thus rejecting it." That question was not under consideration before. Then the Court must find that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts. If your Honor please, the General Mortgage Trustee found no case, [fol. 347] either under Section 77 (e) or any other statute,

where a holder of a secured claim has been required to surrender his claim and the security for the claim, and to accept something else in exchange for his claim over his objection without at least a majority vote of approval from other secured creditors of the same class. We believe that it is not proper for a court under any statute to confirm a plan over such objections without at least a majority vote of approval. That would relate to a reorganization under Section 77 of a bankruptcy composition. It is fundamental that you cannot take security from a man or make a secured creditor release his claim unless a majority think it is fair under the circumstances and vote for it. Here we haven't got that. We have approximately eighty per cent of the bondholders voting against this. That in itself is evidence of the reasonableness of their rejection. If it were by a smaller vote it would not be nearly as persuasive. This Court must find that they had no reasonable basis, no sound basis, for voting against it, before it can confirm the plan over their rejection even though it was proper before to find the plan fair and reasonable. This is a very serious thing.

Mr. McAllister: Mr. Watts, may I ask you a question? You have said eighty per cent of the General Mortgage bondholders voted against it. That was only about seventeen per cent of the votes.

Mr. Watts: Only about four per cent voted in favor, so it was about four to one voted against the plan.

The Court: What percentage of all the bondholders were represented?

Mr. Watts: That is, those that voted for and against [fol. 348] the plan?

Mr. McAllister: I think, your Honor, it is about twenty-one per cent of all of the bondholders voted either for or against the plan.

Mr. Gibson: May I supplement that, your Honor? The exact figures are that of the outstanding General Mortgage bonds less than twenty per cent, approximately seventeen per cent, voted against the plan, and of all publicity held bonds, which was your Honor's exact question, 4.64 per cent voted for the plan, only 4.64 per cent, and could I say that by not answering Mr. Watts at this moment we do not want to be in the position of seeming to agree to any of the argument he has made?

The Court: I understand. We will take the testimony and discuss this later. Finished with your witness?

Mr. Watts: Your Honor, may I ask the witness to read these provisions before you make your ruling, so we will have them in the record?

The Court: What provisions?

Mr. Watts: The provisions of the proposed statute and the sections of the Executive Committee report.

The Court: I don't think I am interested in that. I don't think proposed legislation is any evidence at all or should have any influence on the Court in the decision of the case, unless you bring it home to each individual bondholder and have him here and have him testify he was influenced by the argument in support of the bill or the provisions of it.

Mr. Homire: Your Honor, right at that point I think it would be desirable to point out that the statute provides that the Court fail to confirm the plan if the rejection was reasonable in the light of the rights and interests of the [fol. 349] bondholders so voting to reject, not in the light of their rights at some future time or following the passage of some future legislation. Even if they knew all about this legislation it would not be ground for your Honor sustaining their vote of rejection.

Mr. Watts: Your Honor, that goes just part way through that section. It is "in the light of the respective rights and interests of those rejecting and all the relevant facts," and we believe that the fact that there was such legislation pending was a relevant fact. It might influence them. They were considering all reasonable evidence.

The Court: I suppose you could go through the bills of Congress and find bills about everything. I don't think this has any bearing at all.

Mr. Watts: All we are urging is that the bondholders when they voted knew that such a bill was pending, that it had been unanimously approved by the Committee on the Judiciary, and we believe that has a bearing on whether or not the rejection was reasonable.

The Court: What evidence have you that it was approved by the Judiciary Committee? You haven't any members of the Judiciary Committee here, have you?

Mr. Watts: I have an official publication here.

The Court: I don't think I am interested in that, going into all the matters proposed before the Congress and some

committee. If you want to submit it in a brief I shall be glad to consider it.

Mr. Watts: And to obtain your ruling I would like to offer the exhibit which has been marked City Bank Farmers Trust Company Exhibit 12 for identification—Exhibit 13 for [fol. 350] identification.

The Court: I will sustain the objection.

Q. Mr. Kennedy, do you know when the present plan was submitted to the holders of the General Mortgage bonds for acceptance or rejection?

A. April of this year I understand.

Q. If I tell you the official——

A. It was April 26, 1944.

Q. Does that refresh your recollection?

A. Yes sir.

Q. If I tell you that in the paper submitting the plan it was stated that the votes must be in by June 10, 1944, would that refresh your recollection on that?

A. Yes sir.

Q. Do you know if any notice regarding the introduction of the Hobbs bill appeared in the daily press?

A. It was covered pretty well in the financial page of the papers that I read. That is as far as my knowledge goes.

Q. Do you know whether the bill was the subject of discussion among persons interested in railroad reorganizations generally?

A. Yes, it was.

Q. In view of the pendency of the bill, the nature of its provisions, in your opinion was the vote of the General Mortgage bondholders in rejecting the plan reasonably justified?

A. I would say it was reasonably justified——

Mr. Gibson: That is the same question.

The Court: What was the question?

(Question read.)

The Court: Objection sustained.

Mr. Watts: If your Honor please, that is all the questions I have of this witness.

The Court: Cross-examination, gentlemen?

[fol. 351] Cross-examination.

By Mr. Gibson:

Q. Mr. Kennedy, your Exhibit 10 or City Bank Farmers Trust Company's Exhibit 10 refers to the insurance Group plan as originally proposed. Will you tell me whether or not it is a fact that in that plan the Refunding and General Mortgage bondholders and the holders of all bonds senior in position to them, or equal in position to them, if there are any, were recognized to the full amount of their total claim in preferences, or whether——

Mr. Watts: I think you made a mistake in that, Mr. Gibson.

Mr. Homire: Are you referring to the General Mortgage?

Q. I again state to you as a matter of fact, Mr. Kennedy, that aside from the General Mortgage bonds every bondholder received in the Insurance Group plan the total amount of his claim, the total amount of his claim or better?

A. I think that is true.

Q. Is it not also true in the second Insurance Group plan the senior bondholders received more advantageous treatment than they finally did in the plan now before the Court?

A. I can't answer that, Mr. Gibson. I haven't given any particular consideration to the treatment accorded to other bondholders as among themselves or in total.

Q. If I would state to you as a matter of fact that a larger allocation of new First Mortgage bonds was made in that plan to existing senior creditors, would you be able to deny that?

A. No, I would not. I would not be able to express any [fol. 352] opinion on it at all.

Q. So it follows that the General Mortgage bondholders are not the only ones who didn't get bonds much as they hoped they might; isn't that true?

A. I don't know, Mr. Gibson. Are you asking me to state what may——

Q. If those premises are right, the conclusion is right; isn't that so?

A. That is true.

Q. In your City Bank Exhibit 10, I believe it is, the percentages are shown on the total claim of General Mortgage

bonds recognized in the new common stock allocation. Is it not true that that percentage is computed on the basis of total claim, and not on the basis of principal amount?

A. Yes.

Q. Is it not true that from that it would necessarily follow that the mere lapse of time would itself reduce all percentages even if no change were made in the allocation?

A. Yes.

Q. Is it not true that the General Mortgage bonds are the most junior security that is recognized in the plan?

A. Yes sir.

Q. Is it not also true that the most junior claim is not always allowed interest?

A. Yes, the junior recognized security in general takes what is left.

Q. Is it not also true that if that percentage were computed on the basis of principal amount in general it would be 14.61 instead of 10?

A. I think that is true.

By Mr. Hodges:

Q. Is it not also true, Mr. Kennedy, that taking your Exhibit 11, column III, and the percentages beginning at the bottom of that column with the ten per cent and going upwards, that your percentages would be altered if they [fol. 353] had reference to the original claim of the General Mortgage, unaffected by the accumulation of interest?

A. Yes.

Q. And you haven't figured it on that basis of the principal of the General Mortgage claim as it existed on November 1, 1935?

A. I haven't, Mr. Hodges. I don't know if anyone else has or not.

Q. Are you acquainted with the amount in principal, the principal amount of the senior claims against this debtor as of November 1, 1935, senior to your General Mortgage?

A. Well, I have seen the figures, Mr. Hodges, but I haven't got it in mind.

Q. Accuracy is not necessary to this inquiry.

A. Well, my memory is notoriously poor, Mr. Hodges, and I wouldn't want to hazard a guess. (Referring to document) Well, something in excess of $100,000,000.00 I would say from this computation, that is, principal amount.

Q. That is the principal amount of what might be called senior claims in the aggregate of $101,970,000.00?

A. Yes sir.

Q. And that figure represents the principal amount of all of the bond issues in the hands of the public and all of the bonds pledged and the obligations for which they were pledged?

A. That is my understanding.

Q. And that the total will amount to $101,000,000.00 or approximately $102,000,000.00? That is close enough for our purposes.

A. Yes sir.

Q. And on that day, November 1, 1935, there were $102,000,000.00 of obligations ahead of you. I am speaking of you now as a representative of the General Mortgage bond-[fol. 354] holders. Have you looked at this record in these proceedings to see what valuations have been used by the Commission?

A. Yes, I have.

Q. They have expressed something in terms of capitalization, and do you take it that that is the way they have of expressing some idea of value?

A. You mean the total capitalization?

Q. Yes.

The Witness: May I have that question, please?

(Question read to the witness.)

A. Yes.

Q. So that for the purposes of this questioning I will use capitalization in the sense of value. Do you know of any capitalization that they suggested at any time in any plan that was less than $140,000,000.00?

A. You mean for this property?

Q. Yes, for this railroad.

A. No, sir, I don't.

Q. And what was the principal of your debt on November 1, 1935?

A. In the neighborhood of twenty-nine million.

Q. Twenty-nine million. So, taking your twenty-nine million to the one hundred and one million ahead of you, there was one hundred thirty million of debts to be compared with the one hundred and forty million capitalization?

A. That is correct.

Mr. Gibson: By that you mean principal amount?

Mr. Hodges: I mean principal amount of debt on November 1, 1935.

Q. So that if this plan of reorganization had been put into effect on November 1, 1935, on the basis of any valuation that has been used in this proceeding your claim would [fol. 355] have received at least 100 per cent in new securities or shares under that capitalization?

A. I should judge so, yes, sir.

Q. Now we are nine years or thereabouts later. How much indebtedness are they putting ahead of you now in this plan of reorganization which is now before the Court?

A. (Referring to documents) I should say about $140,000,000.00. That is Rio Grande securities alone, not the Denver & Salt Lake.

Q. Well, using a figure comparable with the first figure you used. I think that first figure you used——

A. One hundred and forty million.

Q. That one hundred and two million was a Rio Grande figure without the Salt Lake?

A. That is right.

Q. Now they are putting $140,000,000.00 ahead of you. So that through lapse of time they have allowed to be accumulated on creditors' claims ahead of you and other creditors some thirty odd million dollars?

A. Yes, sir.

Q. And that has reduced your distributive share in the securities of this reorganization?

A. It has unless the capitalization is increased to allow for the improvements they have made, also been made during this receivership period, which have added to the value of the property, and certainly have added very substantially to its earning power.

Q. But they have not increased the capitalization over and above the original capitalization by more than $7,000,000.00?

A. That is correct, sir.

Q. And the result is that you are shoved down below thirty million more than would have been the case on November 1, 1935?

[fol. 356] A. Yes, sir, that is correct.

Q. So that during this administration the relative rights of creditors have been shifted and adjusted by the accumulation of interest on the claims senior to yours?

A. That has been the effect.

Q. That is clearly the effect, is it not?

A. It seems so to me, Mr. Hodges. I am not answering any question that has a question of law in it.

Q. There is no question of law in it. This is just the question of mathematics and the fact I wanted you to put on the record. So that starting out on November 1, 1935, you would have securities representing $100,000,000.00 of the capitalization of this new company, and today you are offered securities of a junior type representing a little over $4,000,000.00 or approximately $5,000,000.00; is that not so?

A. Yes, sir.

Q. And that latter figure is fourteen per cent of your original claim?

A. Yes, sir.

Q. And during this time this property has been improved very substantially?

A. Yes, sir.

Q. Do you know the figures of the improvement program, what has been invested?

A. Yes, there has been approximately thirty-seven million, as I recall, invested from the date of receivership to the date of December 1, 1943.

Q. Now, I would like to get very clearly with you what you meant by your discussion with the Court as to these earnings. We have before us for every year a statement of net income which you have seen I take it?

A. Yes, sir.

Q. For every year of the operation of these trustees, [fol. 357] and before reaching that figure of net income, all maintenance expenses are deducted from income; is not that true?

A. That is correct.

Q. So we have a series of years in which we have some net income, except one year I think we have a deficit?

A. You mean no income available for taxes I presume?

Q. Available for taxes, not available for interest.

A. Yes.

Q. When you say that the earnings belong to the creditors, you were talking of that income over and above all those expenditures?

A. Including maintenance, yes, sir.

Q. Yes; including maintenance. Now, you were not talking about the question of the Court's policy in improving the property and using the income to pay for that im-

provement. You were not discussing that at all except as an element of improvement; isn't that true?

A. Yes, sir.

Q. So that if any of this income over and above that net income is subject to disposition by the Court without accounting to the creditors, you didn't intend to pass on that at all?

A. Oh, no, certainly not.

Q. Now, in this period of improvement of this property I understand your testimony to be that there has been an actual improvement in the useful value of this property. Maybe I shouldn't use the word "value." In the utility of this property.

A. Yes, sir, I think very definitely that is true. To form any other conclusion you would have to conclude that the trustees had not known their business, didn't know what they were doing.

Q. The other conclusion would be that the expenditures were unjustified?

A. Yes.

[fol. 358] Q. Now, have you given consideration to a program of abandonment of rail during that period?

A. Abandonment of line?

Q. Yes.

A. I know that lines have been abandoned. I haven't any schedule of it, no sir.

Q. Have you looked at it enough to give some opinion as to whether the abandonment of these lines has improved the general efficiency and utility of the plant?

A. I wouldn't have to look at it, Mr. Hodges. I know perfectly well that the Interstate Commerce Commission approves the abandonment of a line which means that line has been a decided drain on the system, and therefore the abandonment has meant an improvement to the property.

Q. And that has been accepted as a sound proposition, has it not?

A. Yes.

Q. And then one other item occurred to me as you were testifying. You are aware, are you not, that these expenditures for what we will call additions and betterments were made during what we call the depression period or during the period of operation by these trustees?

A. During the period of operation of these trustees, yes sir.

Q. Do the men in your profession have a common understanding as to what the depression period is or was?

A. I am afraid not, sir.

Q. You can't cut it off and say the beginning was in the year 1930 or 1931?

A. No sir, because it was different for different industries, and that would always be the case. Of course, we know when the worst of the depression was, and that was in the period of 1932 say through 1935. About the middle of 1936 conditions began to improve and continued to improve through 1937 to August or September, 1937, and [fol. 359] then began to drop off again.

Q. So that these expenditures which were made between 1935 and we will say 1941, is it fair for me to say they were made during the depression period?

A. I wouldn't include 1941. I would take it through 1939.

Q. Now, does the reflection of the expenses that were incurred in carrying out such a program—does that burden fall comparatively more heavily in years of that kind?

A. You mean larger in proportion to the gross revenues, of course.

Q. And they show more emphatically in the earnings of those years?

A. Yes, dollar for dollar, that is, they do.

Q. Now, I don't know whether you want to discuss this point or not, but I want to bring it out from examination. I asked you if you knew anything about the formula used here, and you said no, and you didn't want to study it or didn't want to know it. I think there are some simple facts that you may call to the Court's attention. You do know that a test year was used, and a formula for the distribution of earnings was arrived at?

A. Mr. Hodges, all I know, or I did know considerably more about it at the time, but the only thing that I know is what I have learned from those statements of the Interstate Commerce Commission which disclosed the formula that was used. I can't discuss anything which is not in this formula.

Q. I think there are some things which you can make quite clear to the Court. I won't ask your whether the plan is good, bad or indifferent, because you haven't undertaken to determine that, but you do know from an examination of the report that a formula was used?

[fol. 360] A. Yes. I don't know how much remained of it after all the adjustments were made, but I know there was a basic formula.

Mr. Gibson: Would it not be sufficient, your Honor, that the witness has said he doesn't know?

The Court: Doesn't know?

Mr. Gibson: Doesn't know the answer to the question that is being repeated over and over by the counsel.

The Court: I think we should know it if he doesn't know.

Mr. Hodges: I will tell you what I want to prove. Maybe they will admit it. That in this formula——

The Court: What formula; the Wyer formula?

Mr. Hodges: It was originally proposed by Mr. Wyer. It was employed and adopted by the Interstate Commerce Commission, and it didn't stand on the authority of Mr. Wyer's testimony. It stood upon its adoption by the Interstate Commerce Commission, and it was a formula which is used by the Interstate Commerce Commission for the distribution of securities under this plan.

The Court: Did the Commission say they followed that formula?

Mr. Hodges: That is what I take it they say. I will refer you to the page.

The Court: All right.

Mr. Hodges: Now, it is perfectly plain that in making up that formula there is $126,000,00 of income from the Junction bonds or from the Junction property included in [fol. 361] the formula, and that the ratios of distribution are determined after putting that $126,000.00 into that formula. Now, when you eliminate the Junction bonds you eliminate that $126,000.00 from the formula, and you make the distribution to everybody less, and it is just as plain as day and it is purely a matter of mathematics, and I can argue it from this record, but I thought I would like to have this man clarify it as he could do if I called it to his attention. That is all.

Mr. Gibson: Wouldn't his argument on the record be equivalent to having it from the witness?

The Court: Mr. Hodges has ceased his examination, so we are through with that.

Mr. Watts: Before the witness goes down from the stand, it is understood, is it not, that there is no need for noting our objections to the Court's rulings or our exceptions, so that the exception is saved?

The Court: Yes.

Mr. Watts: I would like to call Mr. Ralph E. Morton.

RALPH E. MORTON, being called and sworn as a witness on behalf of the City Bank Farmers Trust Company, testified as follows:

Direct examination.

By Mr. Watts:

Q. Mr. Morton, will you give your name and address?

A. R. E. Morton, 22 Williams Street, New York City.

Q. Mr. Morton, what is your business?

[fol. 362] A. I am one of two vice-presidents in charge of the Corporate Trust Reorganization Department of the City Bank Farmers Trust Company, having been assigned to that department in May, 1927.

Q. Do you have as part of your personal work in that department the administration of trusts created by railroad mortgages?

A. I do.

Q. Has City Bank Farmers Trust Company had many railroad mortgage trusteeships?

A. It has. At the present time I am administering approximately seventy-five railroad issues in my division of the department.

Q. Do you know if the trust company, either under its present name or its former name of The Farmers Loan & Trust Company, has taken part in many railroad reorganizations?

A. It has.

Q. In the course of the work you personally have done in connection with the reorganization of corporations which have given mortgages to the trust company, have you been consulted frequently by the holders of the securities with respect to the merits of plans of reorganization or readjustment which have been from time to time proposed for the securities?

A. I have in a great many cases.

Q. Do the holders of railroad bonds frequently give you their views with regard to the fairness of proposals for reorganization or readjustment of railroad debt?

A. They do where reorganization is involved, very often at some length.

Q. They do that by letter or telephone or by calling upon you?

A. Very often by calling either personally or through legal or financial representatives or railroad experts, and also by telephone inquiries and letters.

[fol. 363] Q. Will you describe briefly some of the railroad reorganization proceedings in which you personally have participated?

A. In the last ten years I have been working on the Chicago, Milwaukee, St. Paul & Pacific reorganization, Chicago & North Western, the Erie, New York, New Haven & Hartford, the Minneapolis & St. Louis, Savannah-Atlanta, the Missouri Pacific, and I think that covers a fair part of the list.

Q. And in all those cases have bondholders consulted with you and given you their views in regard to proposals that have been made from time to time?

A. They have without exception.

Q. Mr. Morton, are you familiar with the exhibit which was introduced this morning as City Bank Farmers Trust Company Exhibit 10 which is a table of income available for interest and interest upon certain senior securities?

A. Yes, I am.

Q. And are you also familiar with the table which was introduced as City Bank Farmers Trust Company Exhibit 11 which refers to some eleven reorganization proposals which have been made in this case as well as the provision made for the claims of the General Mortgage bonds in those proposals, and set alongside of them certain figures in regard to the current earnings of the debtor available for interest in the years in which the proposal was made, as well as the net situation up to the last previous December 31st prior to the date on which such proposal was made with respect to such earnings available for interest as contrasted with such senior interest requirements?

A. I am.

Q. And have you been from time to time, as the various figures were available, in a general way familiar with all the figures which are for convenience set forth in tabular [fol. 364] form on those exhibits?

A. I have.

Q. And have you ever considered the relationship between the several treatments proposed for the General Mort-

gage bondholders from time to time as contrasted with what appear to be the current earning situation of the debtor at the time those proposals were made?

A. Yes, I have.

Q. And likewise have you considered what the net result of operations to date was to the last previous date as to which cumulative figures were available, say the last December 31st?

A. Well, I have been following the earnings monthly, Mr. Watts.

Q. From your communications from bondholders, whether in the form of personal visitations, telephone conversations or letters, do you believe that at least some of the bondholders have considered the proposals made for the General Mortgage bonds in the light of those figures?

A. Oh, I am certain they have.

Q. In your opinion does the current earning situation of a railroad generally have any bearing upon the reasonableness of a proposal to the creditors of that railroad, particularly where it is a proposal that such creditors should accept in a plan for reorganization securities different from what they hold?

A. Well, in my opinion the earnings have some bearing.

Q. And does the result of operations to the last practicable date have a bearing upon the reasonableness of the proposal made?

A. Yes, I think so.

Q. Did you, Mr. Morton, or anyone else in the Corporate Trust Department of the City Bank Farmers Trust Company make any recommendation to any holder of General [fol. 365] Mortgage bonds as to how they should vote on this plan of reorganization?

A. The City Bank Farmers Trust Company as Trustee under this General Mortgage made no recommendation to any bondholder as to whether he should vote to affirm or reject the plan.

Q. Can you state briefly why you followed that policy?

A. Well, we had been making recommendations before the Commission and Court over a period of years on behalf of bondholders. We had been approached I suppose a half dozen times by various groups of bondholders who were giving consideration to the formation of a protective committee for the bonds. We have offered them all encouragement in each case to go ahead with the formation of the

committee. After the plan was approved by the Court we thought that it was only appropriate to let the bondholders decide on the basis of their individual circumstances as to whether or not they wished to accept or reject the plan.

Q. So the vote of 79.33 per cent of the General Mortgage bondholders who voted to reject the plan was not based in any way upon any recommendation by the Mortgage Trustee that they should vote against the plan?

A. It was not.

By the Court:

Q. What did you mean when you said by their individual situation? What did you mean by that?

A. Some of these bondholders, sir, have been holding bonds which cost them upwards of par. On the other hand, there has been a speculative interest in the bonds, and in some cases some of the bondholders had a substantial profit in the bonds even at the very low price at which they were [fol. 366] selling, and we didn't deem it appropriate in this instance to suggest to any bondholder how he should vote on the plan. There was a good deal of pressure brought to bear on us to appeal from the approval order. In fact, several substantial bondholders made demands on us to that effect. In those cases we indicated that if the bondholders cared to organize and to direct us to appeal and furnish suitable indemnifications under the general provisions of the mortgage, that we, of course, would comply with their direction, but otherwise we thought it was appropriate for the bondholders to express their opinion on the plan on the ballot.

Q. When you spoke of their individual situation that would mean each bondholder should decide from his own financial situation, and not from the good of the company or the reorganization plan?

A. Well, I think he probably would decide on the basis of what he felt was his fair and equitable interest in the situation. It is conceivable that a bondholder who bought these bonds at two, when they moved up to five might feel it was a good plan.

Q. Did they ever sell them at two?

A. I am under the impression they sold that low. At least they sold between two and three, but with these very drastic plans of the Commission which have come out

very recently, the price of the bonds dropped very radically.

Q. He would be interested then whether he had a profit, and not whether it was for the good of the property? His view would then be influenced by whether he bought it at the higher price?

A. I don't know that I should endeavor to go into his motives.

Q. That is what Mr. Watts is asking you, what interest [fol. 367] these people have in voting for the plan.

A. Well, we didn't go into that. That was my answer to his question, sir.

The Court: All right. Go ahead.

By Mr. Watts:

Q. Did the General Mortgage bondholders ever come to you to tell you their views upon the plan, and to urge you to appeal from the order approving the plan, or in any cases did they tell you their views with regard to their prospective vote on the plan?

A. Yes, but I don't believe a single bondholder advised how he was going to vote on the plan.

Q. Mr. Morton, on the basis of the facts which for convenience are arranged in tabular form on those two exhibits, and on the basis of all the information that was available to the bondholders from time to time, was it in your opinion reasonable or unreasonable for the bondholders to vote to reject the plan?

A. Yes, reasonable.

Mr. Gibson: Your Honor please, an objection to the preceding question of the preceding witness was sustained.

Mr. Watts: No, it was not sustained.

Mr. Gibson: I object on the ground that the question is calling for an opinion on an issue for the Court to decide.

The Court: Objection sustained.

Q. Mr. Morton, did you hear the testimony given by Mr. Kennedy a short time ago with regard to the Hobbs bill and the report of the Committee on the Judiciary on the Hobbs bill?

A. I did.

Q. Are you also familiar in a general way with the various texts of this bill as from time to time introduced in the [fol. 368] House of Representatives?

A. I am.

Q. And are you familiar with the report on the bill?

A. I am.

Q. From your contact with holders of General Mortgage bonds do you know whether at least some of the holders of General Mortgage bonds were prior to June 10, 1944, familiar with the provisions of the Hobbs bill?

A. They were.

Q. And with the reports on the contents of the report of the Committee on the Judiciary?

A. They were.

Mr. Watts: Your Honor please, with this additional testimony as to the Hobbs bill and the report of the committee having been familiar to at least some holders of General Mortgage bonds, I should like to now reoffer the documents which have been marked Exhibit 12 and Exhibit 13 for identification.

The Court: Well, the evidence is that they were familiar with it, but there is no evidence whether they approved of it or believed in it.

Mr. Watts: No, sir, I don't believe that is material.

The Court: I don't think it is material unless they do give evidence one way or the other.

Mr. Watts: I think it is material that they knew it was pending. I don't want to get it in for the reason they approved of it or didn't approve of it. I think it is evidence as to the reasonableness of their vote.

The Court: Not unless you show they approved of it or that was the reason for their voting. This witness' testimony is that some of these bondholders were speculating, and they bought the bonds at $2.00 and they went up to five, [fol. 369] and they wanted to get their profit on it.

Mr. Watts: I believe it is the function of this Court at the end of this hearing to determine for itself whether or not the action of the General Mortgage bondholders in voting to reject the plan was or was not reasonably justified in the light of their relevant rights and interests and in the light of the relevant facts, and I believe for your Honor to form an informed judgment on that question it is necessary for you to know just what facts there were available for these bondholders at that time.

The Court: When these bondholders come in I will be glad to. I do not think it is material. The Court has to reach its own judgment on the financial situation and the provisions of the plan.

Mr. Watts: We conceive this to be a relevant fact, your Honor please, that the statute refers——

The Court: I have read articles in favor of the Hobbs bill, and some are much opposed to it. I hope that neither of those articles will influence me in this case.

Mr. Watts: I want to make it very clear that in offering this testimony the General Mortgage Trustee does not offer any views on the Hobbs bill.

The Court: What is the object, then?

Mr. Watts: I am sorry. I have tried to explain. It——

The Court: You want it to have some influence on the Court because you have offered it.

Mr. Watts: The only influence I want it to have on the Court, sir, is to have you consider that the General Mort-[fol. 370] gage bondholders or those of them who kept current with what was happening in the financial world and in Congress probably knew, because of the publicity given the matter in the press, that the Hobbs bill was pending at the time they were going to vote on a plan which cut them down to ten per cent of their claim and forever forfeited ninety per cent, or the rest of their claim, that there was no unanimous approval of the plan, and that the report of the Judiciary Committee on the Hobbs bill specifically referred to this Denver case as a glaring example of what was happening to junior security holders, and that the bill provided that if the bill became law, all the pending reorganization plans would become subject to it. I believe knowing that was a very material fact in considering whether it was reasonable or not for a bondholder to vote for or against the plan.

The Court: I can't agree with you.

Mr. Watts: Your Honor, I have no other questions of this witness.

Cross-examination.

By Mr. Homire:

Q. Mr. Morton, have you any information as to how many of the General Mortgage bonds now outstanding are in the hands of the same holders who held them when the reorganization proceeding commenced?

A. No, I haven't. I suppose a check of the ballots against the debtor's original list might show that, but the company itself paid interest on the bonds prior to default, and we haven't happened to do that, nor have we seen the list of the people balloting.

[fol. 371] Q. You have no record or information on that?

A. No.

The Court: Anything further of Mr. Morton?

Mr. Keegan: I don't want to ask any questions, but I have an exhibit we discussed the morning I would like to offer now.

(Thereupon a document was marked for identification City Bank Farmers Trust Company Exhibit 9-A.)

Mr. Keegan: Your Honor, we have two exhibits here marked Exhibits 9 and 9-A which we are offering as part of our evidence on the petition for adjustment as the result of the purchase of the Junction bonds. 9-A is a copy of our letter of transmittal and copies of our petition to the Commission, and Exhibit 9 is a letter from Director Sweet of the Commission to us, acknowledging receipt of the petition. In that letter——

Mr. Gibson: We are prepared to make objection to the admission of the letter, and we would prefer to do that before its contents are described by counsel.

The Court: What is the probative value?

Mr. Homire: We think it has no probative value whatever.

The Court: Just a minute. I don't know what he claims for it.

Mr. Keegan: That is what I was going to try to explain. We are contending that our petition for the construction of the plan does not involve changing the valuation or capitalization of the company in any way. It is merely an authorized adjustment within the framework of the [fol. 372] plan, and when Director Sweet acknowledged receipt of the copies of our petition he said in substance, as I remember the letter, that he had received copies of our petition for adjustment within the approved plan as the result of the purchase of the Junction bonds. We think by implication taken in connection with what we will show in our argument the Commission has been doing in other railroad reorganization cases where similar ques-

tions have come up and where they are approving this type of adjustment, that that has some significance on the way they interpret it to find what it is.

The Court: It is an action of the Interstate Commerce Commission. It is not binding upon the Commission in any way.

Mr. Keegan: No, it is not a finding in advance.

The Court: It is not even from the Commission. It is just from the director. I don't know whether this man Sweet is a member of the Commission.

Mr. Homire: He is not a member of the Commission.

The Court: Any objection to this?

Mr. Homire: We object to it.

Mr. Gibson: We object to it.

The Court: Objection sustained. Too far fetched and speculative.

Mr. Keegan: We are ready to proceed with the argument.

(Thereupon a recess of ten minutes was taken.)

Mr. Gibson: Before we proceed further, there is one point we conceive is important to have clarified. In previous hearings before your Honor on matters of general [fol. 373] concern, like the approval of the plan or the affirmance of the Salt Lake Western lease and similar matters, your Honor has made it clear from the bench that the record in all prior proceedings before this Court and the record in all prior proceedings before the Commission in this proceeding are part of the record in this hearing. We think it important that that be clarified here in the same way.

The Court: You mean that the record of the whole proceeding is considered part of this question?

Mr. Gibson: Yes, your Honor.

The Court: I think that is true, and if there is no objection it will be made part of the record.

Mr. Gibson: And could it similarly be ruled that the record at this hearing include all the certification material certified to your Honor by the Interstate Commerce Commission with respect to the balloting on the plan?

The Court: Very well. It is so ordered.

Mr. Gibson: The Clerk has physical possession of those documents here. If I could be permitted to enumerate them I think that would clarify the transcript. As I

understand it, your Honor, the certification material in the custody of the Clerk includes principally four bodies of information. One of them is a certified copy of the order of the Commission dated March 23, 1944, providing the procedure for submission to the creditors, together with exhibits attached to it. The second is a certificate of the Commission dated July 4, 1944, duly reporting to your Honor the results of the submission, and with that certificate there are submitted to your Honor (1) a list of the known holders of bonds of the several classes to whom sub-
[fol. 374] mission was made, and (2) duplicate originals of the various ballots executed by the bondholders. All of that material, we submit, should be made a part of the record at this hearing.

The Court: So ordered.

Mr. Gibson: And may we suggest to your Honor one further point, and that is that the development of the evidence this morning makes it quite clear that the issues presented by the petition of the City Bank and the issues presented by the question of confirmation of the plan, cannot feasibly be separated. Both points are urged in both the objections and the petition filed by the City Bank. We think the argument on both issues should proceed simultaneously.

The Court: Any objection to that?

Mr. Keegan: Now, if your Honor please, we would like to argue the Junction bond issue first. It is a separate question. Mr. Watts will cover our other objections.

The Court: You have two objections?

Mr. Keegan: One petition for adjustment as a result of the purchase of the Junction bonds and one objection to the confirmation of the plan.

The Court: That raises two points?

Mr. Keegan: They raise two points as far as we are concerned. I will cover the narrow issues, and Mr. Watts will cover the balance.

Mr. Homire: We didn't have an opportunity to put on one witness, Mr. Thompson.

The Court: Do you want to call him?

Mr. Homire: Just very, very briefly.

The Court: All right.

[fol. 375] Mr. Hodges: May it please the Court, while you are waiting I have received no notice of anyone's motion asking the Court to confirm this plan. I have assumed that

this hearing was called on the Court's own motion. Am I correct?

The Court: It was set for hearing on order of the Court, yes, and all parties so notified.

Mr. Hodges: I think it was set, but no party moved the Court to confirm the plan.

The Court: You mean there is no motion for the Court to act upon?

Mr. Hodges: I don't mean that, but I wanted to know whether someone had moved the Court. I don't happen to have a copy of such a motion.

The Court: I don't find a copy of such motion.

Mr. Gibson: Your Honor please, we believe that is not a necessary step in the procedure of 77. If the gentleman would be happier, we will so move now.

Mr. Hodges: Oh, that pleases me.

The Court: The order provides that the matter be set for hearing before the Court. That is notice to you all. That is due and sufficient notice to bring the matter up. All right.

Mr. Homire: Mr. Thompson said he would not be able to prepare the data until tomorrow morning.

The Court: Very well.

Mr. Keegan: These exhibits are now marked 14 to 17, and, pursuant to Mr. Gibson's request, we would like to offer those to complete the set. Mr. Gibson states I should go through these to identify them. Exhibit 14 is the income account statement for the month of October.

[fol. 376] The Court: It is not necessary. We understand what they are. Anybody that wants that information may get it.

. . . . . .

Thereupon an adjournment was taken until ten o'clock a. m. Thursday, August 31, 1944.

Pursuant to adjournment the following proceedings were had at ten o'clock a. m. Thursday, August 31, 1944:

Mr. Gibson: If your Honor please, it appears that the papers that have been certified here by the Interstate Commerce Commission as to the submission of the plan to the

creditors do not include the pamphlet that was sent around to all creditors, containing your Honor's opinion and the opinions of the Commission on the plan. We think it is appropriate to have that in the record. I have here one of the official copies.

The Court: My original opinion is in the record.

Mr. Gibson: Yes, your Honor, but this is the submission pamphlet which evidences the way the bondholders were informed. I would like to offer that in evidence.

The Court: It will be admitted.

Mr. Gibson: I suppose it will be convenient to have some way of referring to it, so I suggest Insurance Group No. 1 as the reference.

. . . . . .

[fol. 377] Mr. Watts: I would like to move this Court that the plan be not confirmed, and that it be referred back to the Commission for further consideration.

Mr. Keegan: On this question of requested adjustment within the framework of the plan as the result of the purchase of the Junction bonds, when the arguments of opposing counsel on that point are analyzed we submit that they simply go to a question as to whether the Court has the power to make that adjustment or whether it is an adjustment that the Commission only can make.

The Court: I am convinced, after reading these cases, it is only an adjustment that the Commission can make, and so it would have to go back to the Commission. I don't think I have power to change this allocation.

Mr. Keegan: Well, the Commission can't take the first step.

The Court: I don't think that was a proper procedure in the New Haven case. He said "I am going to do this, and, unless the Commission reverses me, it is going to stand," and I do not believe in that attitude. If I had felt as he did, I would have suggested I make the ruling and then let it be reversed on appeal, and not sort of dare the Commission to contradict it.

Mr. Keegan: But how is the Commission going to take the first step?

The Court: Well, I don't know. They have had this before them. They have had plenty of time to take any step they wished before they sent it to this Court.

Mr. Keegan: It has not been before the Commission since the Junction bonds were purchased.

[fol. 378] The Court: I think the Court of Appeals, if I am wrong, would tell me I should have made that change myself. I think it is really a matter for the appellate court rather than for me to do something and then tell the Commission "I have done this, and I hope you will approve of it," because the jurisdiction of the Commission and of this Court are entirely different. I do not think that both have the same jurisdiction over the same questions under these Supreme Court cases. They very clearly told this Court just what it would have to do under a reorganization plan, and what the duties of the Commission are on the application and on the capital structure. I have nothing to do with the capital structure of this reorganization plan. I simply pass it as a whole and in the view of the light of equitable principles.

Mr. Keegan: When they promulgate the plan they recognize that there are certain adjustments that have to be made.

The Court: As I tried to point out to you yesterday, I do not think this is an adjustment. It is a change in the whole capital structure that you advocate. The first mortgage bonds might come in and say "We are entitled to all these new securities because we have not been paid this bonus." I don't think it is a question to be decided by the Court. I would be very glad to consider any brief or case you want to cite before I pass on it. Does anybody want to file any memoranda or briefs on these questions?

Mr. Keegan: If you do not agree with the New Haven case there is not much point to go further with that.

The Court: I will be glad to have you file a brief on the case.

[fol. 379] Mr. Keegan: From the transcript here of the hearing in September, 1943, Mr. Homire, Colonel Anderson and Mr. Sunderland all argued that if this money was used to purchase the Junction bonds then the only way open was to make this adjustment.

The Court: Well, I can't expect counsel to be consistent in taking different cases.

Mr. Keegan: This is the same case and the same point.

Mr. Homire: That is precisely contrary to the position of that petition, as I said to Mr. Keegan.

The Court: Send the record in and make your argument on it and I will be very glad to consider it.

Mr. Honnire: We feel that the matter has been very fully presented to the Court, and it would be perfectly useless.

The Court: I will have the reporter write out the argument and I will read that, and any counsel may supplement the argument made here within ten days.

Mr. Sunderland: And reply to any brief submitted?

The Court: I don't want any brief. I will make the brief.

Mr. Sunderland: Could you make that a little longer, because we won't reach New York until Monday, and most of the time will be gone?

The Court: I will make that fifteen days. The law requires the Court to file a written memorandum, so if I have any views, that wouldn't serve any purpose today. I will keep an open mind on it until I can read these arguments and any briefs they may want to file, even though they may indicate today they are not interested in so doing.

[fol. 380] Filed United States District Court, Denver, Colorado, Jan. 10, 1945. G. Walter Bowman, Clerk.

[fol. 381]

IN UNITED STATES DISTRICT COURT

CITY BANK FARMERS TRUST COMPANY EXHIBIT 8

The Denver and Rio Grande Western Railroad Company

Interest on Unfunded Debt

	Total	Reconstruction Finance Corp.	Railroad Credit Corporation	Bank Loans	Miscellaneous	Available for Interest on Funded Debt
1943	$664,318	$574,093	$996	$76,042	$13,187	$11,116,576
1942	783,186	574,093	2,659	76,042	130,392	16,529,932
1941	1,593,645	1,372,095	2,709	76,042	142,799	2,910,045
1940	700,017	430,018	2,802	76,333	190,864	2,120,496
1939	692,938	427,674	2,794	76,042	186,428	1,213,582
1938	717,053	427,674	2,441	76,042	210,896	*493,698*
1937	612,305	427,674	4,324	76,042	104,265	*798,596*
1936	538,858	427,679	5,104	76,167	29,903	1,122,333
1935	530,388	427,077	5,921	76,250	21,140	1,929,183
1934	340,259	241,244	7,174	78,771	13,070	2,260,019
1933	258,049	157,817	13,711	83,646	2,875	3,140,746
1932	154,780	65,466	7,597	79,625	2,092	2,739,799
1931	61,838			57,854	3,984	5,142,666
1930	51,041			31,056	19,985	7,068,617
1929	27,649				27,649	8,811,533
1928	2,387				2,387	7,314,899
1927	3,604				3,604	6,472,257
1926	6,283				6,283	7,705,670
1925	18,846				18,846	6,780,296
1924	74,422				74,422	2,394,626

Italics denote debit.

[fol. 382]

IN UNITED STATES DISTRICT COURT

CITY BANK FARMERS TRUST COMPANY EXHIBIT 10

Table Showing Debtor's Income Available for Interest and Interest Requirements for All Securities Senior to General Mortgage Bonds for Each Year During Reorganization Proceedings

	I. Year	II. Debtor's Income Available for Interest	III. Debtor's Interest Requirements for Securities Senior to General Mortgage Bonds Including Interest on Unfunded Debt	IV. Surplus (or Deficit) II minus III
1.	1935 (Nov.-Dec.)	$405,418	$701,818	$-296,400
2.	1936	1,626,179	4,182,219	−2,556,040
3.	1937	−294,880	4,160,664	−4,455,544
4.	1938	10,018	4,179,725	−4,169,707
5.	1939	1,717,298	4,184,227	−2,466,929
6.	1940	2,626,847	4,206,933	−1,580,086
7.	1941	4,358,182	5,169,696	−811,514
8.	Total to 12/31/41	$10,449,062	$26,785,282	$−16,336,220
9.	Average per year to 12/31/41	$1,694,436	$4,348,556	$−2,649,120
10.	1942	$17,180,067	$4,382,701	$+12,797,366
11.	1943	11,766,711	4,368,551	+7,398,160
12.	Total for 42-3	$28,946,778	$8,751,252	$+20,195,526
13.	Average per year for 42-3	$14,473,389	$4,375,626	$+10,097,763
14.	1944	$10,277,000*	$4,357,285*	$+5,919,715*
15.	1944 (for 7 months)	5,992,635	$2,541,745	$+3,450,890
16.	Total for whole period 11/1/35 to 12/31/44	$49,672,840*	$39,893,819*	$+9,779,021*
17.	Average per year for whole period	$5,418,852*	$4,352,052*	$+1,066,800*

* Estimated as to last five months of 1944.

IN UNITED STATES DISTRICT COURT

CITY BANK FARMERS TRUST COMPANY EXHIBIT 11

Table Showing (a) Current Debtor's Income Available for Interest and (b) Surplus (or Deficit) of Total Debtor's Income Available for Interest to Last Previous December 31 *over* Interest Requirements to the Same Date of All Securities Senior to General Mortgage Bonds (Including Interest on Unfunded Debt), All as of the Respective Dates on Which the Several Plans Were Proposed—As Well as the Treatment Proposed for General Mortgage Bonds in the Several Plans.

I.	II.		III.	IV.	V.
	Date of Plan Proposal	Plan	Amount of Common Stock provided per $1000 of Gen. Mortgage claims	Current Earnings (for year in which proposal was made) per year	Accumulated Surplus (or deficit) of earnings *over* "senior" interest to last previous December 31
1.	7/28/36	Debtor's (1)	100% (Pref)	$1,626,179	$−296,400
2.	6/15/37	Insurance Group I (2)	100%	−294,880	−2,852,440
3.	8/12/38	Examiners I (3)	50%	10,018	−7,307,984
4.	7/11/39	ICC I (4)	33⅓%	1,717,298	−11,477,691
5.	4/2/40	ICC II (5)	33⅓%	2,626,847	−13,944,620
6.	1/6/41	"Discussion" (6)	50%	4,358,182	−15,524,706
7.	3/6/41	Court's (7)	32.99%	4,358,182	−15,524,706
8.	8/26/41	Examiners II (8)	33⅓%	4,358,182	−15,524,706
9.	10/8/41	Insurance Group II (9)	47.42%	4,358,182	−15,524,706
10.	7/27/42	ICC III (10)	5%	17,180,067	−16,336,220
11.	6/14/43	ICC IV (11)	10%	11,766,711	−3,538,850
12.	Date of Submission of Plans 4/28/44			10,277,000*	3,859,306
13.	Surplus of earnings over "senior interest" as of 12/31/44 (estimated as to last five months of 1944)				9,779,021*

* Estimated.

(1) Printed Record, Vol. 2, Part IV, Pages 1706–43.
(2) Printed Record, Vol. 3, Part IV, Pages 2885–2943, 2932.
(3) Printed Record, Vol. 4, Part VI, Pages 4120–4197, 4187.
(4) Printed Record, Vol. 5, Part IV, Pages 5047–5200, 5168, App. A.
(5) Printed Record, Vol. 6, Part II, Pages 5815–81, 584–1.
(6) Printed Record, Vol. 7, Part II, Pages 7352–70, 7361.
(7) Printed Record, Vol. 7, Part IV, Pages 7684–99, 7698, Ex. A.
(8) Printed Record, Vol. 8, Part I, Pages 8148–93, 8192, App. A.
(9) App. A in Ins. Group Brief dated 10/8/41 filed with I.C.C.
(10) Printed Record, Vol. 9, Part I, pages 9120–9258.

[fol. 384] IN UNITED STATES DISTRICT COURT

ORDER DENYING PETITION OF CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE OF THE GENERAL MORTGAGE, FOR CONSTRUCTION OF THE PLAN AND FOR OTHER RELIEF—Filed November 25, 1944

In accordance with the Court's "Memorandum of Confirmation of Plan" heretofore filed herein, the Petition of City Bank Farmers Trust Company, as Trustee of the General Mortgage, for Construction of the Plan and for Other Relief, dated March 28, 1944, and filed herein on March 31, 1944, having heretofore been fully presented, is denied.

Dated this 29 day of November, 1944.

By the Court, J. Foster Symes, Judge.

[File endorsement omitted.]

[fol. 385]

IN UNITED STATES DISTRICT COURT

APPENDIX A TO REPORT OF INTERSTATE COMMERCE COMMISSION OF JULY 11, 1939

Finance Docket No. 11002

Denver & Rio Grande Western R. R. Co. Reorganization
Including D. & S. L. and D. & S. L. W.

	Present	Approved Plan						
	Total Debt, with interest accrued to June 30, 1938	Stock, etc.	Undisturbed or extended	First Mtge. 4% Bonds Series A	Income Mtge. 4½% bonds Series A	Preferred 5% stock Par Value $100	Common Stock No par value	
Equipment obligations	$1,795,000		$2,795,000	$	$	$	shares	
R. G. Western first trust 4s	17,316,600				(100%) 17,316,600			
R. G. Western consol. 4s	17,342,000					(100%) 17,342,000		
Junction first 5s	2,308,333				(100%) 2,308,333			
D. & R. G. consol. 4s	39,585,000				(35%) 13,854,750	(25%) 9,896,250	(40%) 158,340	
D. & R. G. consol. 4½s	7,530,760				(35%) 2,635,766	(25%) 1,882,690	(40%) 30,123	
D. & R. G. W. ref. & imp. 5s	14,250,000				(35%) 4,987,500	(25%) 3,562,500	(40%) 57,000	
D. & R. G. W. ref. & imp. 6s	2,450,000				(35%) 857,500	(25%) 612,500	(40%) 9,800	
D. & R. G. W. general mtge. 5s	37,155,800						(33⅓%) 123,786	
R. F. C. notes	11,959,469			(100%) 11,959,469				
D. & Salt Lake bonds	11,234,000			11,443,675(a)				
D. & R. G. W. trustees' certificates	5,000,000			5,000,000				
Reorganization expenses, etc.		1,000,000		1,000,000				
Chase Nat. Bank Loan	1,749,917*		1,749,917					
R. R. Credit Corp. loan, approx.	278,000		278,000					
Unsecured claims, approx.	440,000							
D. & Salt Lake minority stock		460 sh.			46,000			
D. & R. G. W. preferred stock		16,445,600						
D. & R. G. W. common stock		300,000 sh.						
Totals	171,374,879		4,822,917	29,403,144	42,006,449	33,295,940	379,049	

	Approved Plan	
	Principal Amount	Annual Charges
Equipment obligations to be assumed	$2,795,000	$98,243
Note to Chase National Bank to be extended	1,749,917*	69,997
Note to Railroad Credit Corporation to be extended if not paid in cash	278,000	4,170
New first mortgage 4 percent bonds, approx.	29,403,444	1,176,126
Total fixed interest debt	34,226,061	1,348,536
New income Mortgage 4½ percent bonds	42,006,449	
Total debt	76,232,510	
Capital Fund, maximum payment		750,000
Contingent interest		1,890,200
Sinking fund, approx.		105,046
Subtotal		4,093,842
New 5 percent preferred stock	33,295,940	1,664,797
Subtotal	109,528,450	5,758,639
New no-par common stock, shown at $100 a share	37,904,904	
Total	147,433,354	

* With interest as allowed by the court. Note to be extended at 4 percent with new collateral consisting of securities for which the present pledged securities would be exchangeable under the plan.

(a) Amount required for redemption of present bonds.

* Including $249,916.67 of interest to June 30, 1938, computed in accordance with the claim of the bank at 6 percent, from the date when the debtor filed its petition under section 77, as provided in the laws of the State of New York. The plan herein approved provides that the interest to be allowed shall be in the amount approved by the court.

[fol. 386]

IN UNITED STATES DISTRICT COURT

APPENDIX A TO REPORT OF INTERSTATE COMMERCE COMMISSION OF JULY 13, 1942

Approved Modified Plan on the Basis of Consolidation with the Denver & Salt Lake. Pledged Securities Omitted

				New Securities Assigned			
D. & R. G. W.	Claims as of Jan. 1, 1942	Undisturbed or extended	New Money	First Mtg. Bonds 3% fixed interest, 1% prior contingent interest	Income Bonds 4½% contingent interest	Preferred Stock 5%	Common Stock $100 per value
Equipment obligations	$9,139,605	$9,139,605					
R. G. West. first-trust 4's	19,443,200			71% $13,804,672	29% $5,638,528		
R. G. West. consol. 4's	19,453,200				6% 1,167,192	69% $13,422,708	25% $4,863,300
R. G. June. first 5's	2,658,333			74% 1,887,416	29% 770,917		
D. & R. G. Consol. 4's	44,362,500			23% 10,203,375	11% 4,879,875	22% 9,759,750	44% 19,519,500
D. & R. G. Consol. 4½'s	8,535,925			23% 1,963,263	11% 938,952	22% 1,877,903	44% 3,755,807
Refunding & Imp't. 5's	16,350,000			18% 2,943,000	8% 1,308,000	21% 3,433,500	53% 8,665,500
Refunding & Imp't. 6's	2,870,000			18% 516,600	8% 229,600	21% 602,700	53% 1,521,100
General mortgage 5's	42,057,755						5% 2,102,888
Chase Nat. Bank note	* 2,068,458	* 2,068,458					
R. R. Credit Corp. note	265,194	265,194					
R. F. C. notes	13,377,209			4,802,040	6,983,568	1,591,601	
Trustees' certificates	5,000,000		$**2,250,000				
Unsecured claims	* 440,000	no equity					
TOTALS, D. & R. G. W.	$186,021,379	$11,473,257	$2,250,000	$36,120,366	$21,916,632	$30,688,162	$40,428,095

Denver & Salt Lake			
Stock held by public	4,111 shares	Assigned 411,100 shares of new preferred stock	411,100
First mortgage 4's	1,500,000	1,500,000 assumed as to interest	
Income 6's	9,734,000	9,734,000 interest modified and assumed	$31,099,262

* Subject to adjustment.

** Provides for payment of $1,250,000 of trustees' certificates (balance to be paid in cash), and $1,000,000 for non-assenting D. & S. L. income bonds; approximate.

	New securities to be issued for pledge as collateral			
	First Mtge. bonds	Income bonds	Preferred stock	Common stock
Chase Nat. Bank note, extended	$1,495,044	$664,464	$1,744,218	$4,402,074
Railroad Credit Corp. note, if extended	197,938	94,666	189,332	378,664

[fol. 387]

Appendix A (Cont'd)

Capitalization and Annual Charges

	On basis of consolidation with Denver & Salt Lake		D. & R. G. W. without D. & S. L.	
	Principal	Annual charges	Principal	Annual charges
Equipment conditional sale agreements, 1941	$2,667,605	$41,979	$2,667,605	$41,979
Equipment trust I, 1941	1,260,000	30,000	1,260,000	30,000
Other equipment trusts	5,212,000	121,853	5,212,000	121,853
Total equipment obligations	$9,139,605	$193,832	$9,139,605	$193,832
Chase National Bank note	2,068,458	44,851a	2,068,458	44,851a
Railroad Credit Corp. note	265,194	2,652	265,194	2,652
R. F. C. claim (see plan)			13,377,209	535,088
Loan for new money	2,250,000	90,000	1,250,000	50,000
Denver & Salt Lake first mtg. bonds, 4% int.	1,500,000	60,000	—	—
Denver & Salt Lake income bonds, 3%–1% int.	9,734,000	292,020	—	—
	$24,957,257	$683,355	$26,100,466	$826,423
New first-mortgage bonds, 3%–1% int.	36,120,366	1,083,611	31,318,326	939,550
Total fixed interest	$61,077,623	$1,766,966	$57,418,792	$1,765,973
Capital fund, maximum payment		750,000		750,000
Prior contingent interest, 1%		473,494b		328,133bb
Sinking fund for first mtg. bonds, ½ of 1%		180,602		156,592
		$3,171,062		$3,000,698
New income bonds, 4½%	21,916,632	1,009,185d	14,933,064	694,925e
Sinking fund for income bonds, ¼ of 1%		54,792		37,333
Total debt, interest, payments to funds	$82,994,255	$4,235,039	$72,351,856	$3,732,956
New 5% preferred stock, par value $100	31,099,262	1,554,963	29,096,561	1,454,828
New common stock, par value $100	40,428,095		40,428,095	
Total capitalization	$154,521,612		$141,876,512	

Distribution of New Securities per $1000 of Present Bonds With Accrued Interest

	First mtge. bonds	Income bonds	Preferred stock	Common stock
R. G. W. firsts	$13,804,672	$5,638,528		
	908 80	371 20		
R. G. W. consols		1,167,192	$13,422,708	$4,863,300
		77 40	890 10	322 50
June. firsts	1,887,416	770,917		
	943 71	385 46		
D. & R. G. consol. 4's	10,203,375	4,879,875	9,759,750	19,519,500
	299 00	143 00	286 00	572 00
D. & R. G. consol. 4½'s	1,963,263	938,952	1,877,903	3,755,807
	307 63	147 12	294 25	588 50
R. & I. 5's	2,943,000	1,508,000	3,433,500	8,665,500
	245 25	109 00	286 13	722 12
R. & I. 6's	516,600	229,600	602,700	1,521,100
	258 30	114 80	301 35	760 55
General 5's				2,102,888
				70 55

a. Fixed interest on the $1,495,044 of new first-mtge. bonds assigned as part of the collateral for new note to Chase National Bank.

b. Comprising prior contingent interest on:

New first-mtg. bonds	$36,120,366—	$361,204
New first-mtg. bonds assigned as part of collateral for new note to Chase National Bank	1,495,044—	14,950
D. & S. L. income bonds	9,734,000—	97,340
		$473,494

bb. Comprising prior contingent interest on:

New first-mtg. bonds	$31,318,326—	$313,183
New first-mtg. bonds assigned as part of collateral for new note to Chase National Bank	1,495,044—	14,950
		$328,133

d. Comprising contingent interest on:

New income bonds	$21,916,632—	$ 986,248
New income bonds assigned as part of collateral for new note to Chase National Bank (only so much as necessary to fill out 4% interest on the note)		22,937
		$1,009,185

e. Comprising contingent interest on:

New income bonds	$14,933,064—	$ 671,988
Part of interest on new income bonds assigned to Chase National Bank note, as in d		22,937
		$694,925

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Appendix B

Approved modified Plan without consolidation with the Denver & Salt Lake. Pledged securities omitted

D. & R. G. W.	Claims as of Jan. 1, 1942	Undisturbed or extended	New Money	New Securities Assigned: First Mtg. Bonds 3% fixed interest 1% prior contingent int.	Income Bonds 4½% contingent int.	Preferred stock 5%	Common stock $100 par value
Equipment obligations	$9,139,605	$9,139,605					
R. G. West. first-trust 4's	19,443,200			71% $13,804,672	29% $5,638,528		
R. G. West. consol. 4's	19,433,200				6% 1,167,192	69% $13,422,708	25% $4,863,300
R. G. June. first 5's	2,658,333			71% 1,887,416	29% 770,917		
D. & R. G. consol. 4's	44,362,500			23% 10,203,375	11% 4,879,875	22% 9,759,750	44% 19,519,500
D. & R. G. Consol. 4½'s	8,535,925			23% 1,968,263	11% 938,952	22% 1,877,903	44% 3,755,807
Refunding and Imp't. 5's	46,350,000			18% 2,943,000	8% 1,304,000	21% 3,433,500	53% 8,665,500
Refunding and Imp't. 6's	2,870,000			18% 516,600	8% 229,600	21% 602,700	53% 1,521,100
General mortgage 5's	42,057,755						5% 2,102,888
Chase Nat. Bank note	* 2,068,458	*$2,068,458					
R. R. Credit Corp. note	* 265,194	265,194					
R. F. C. notes	*13,377,209	13,377,209	(see note)				
Trustees' certificates	5,000,000		*$1,250,000				
Unsecured claims	* 440,000	no equity					
TOTALS, D. & R. G. W.	$186,021,379	$24,850,466	$1,250,000	$31,318,326	$14,933,064	$29,099,564	$40,428,095

Denver & Salt Lake securities,
Undisturbed:
- First mortgage 4's 1,500,000
- Income 6's 9,734,000
- Stock held by public 4,111 shares

* Subject to adjustment.

Note: R. F. C. claim to be provided for by depositing the pledged securities in escrow for a specified period, the receipts from sales, dividends, and interest to be applied first to the payment of interest on the claim of $13,377,209 at 4 percent per annum, any excess to be applied to reduction of principal. For complete details, see plan.

New securities to be issued for pledge as collateral

	First Mtge. bonds	Income bonds	Preferred stock	Common stock
Chase Nat. Bank note, extended	$1,495,044	$664,464	$1,744,218	$4,402,074
Railroad Credit Corp. note, if extended	197,938	94,666	189,332	378,664

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Appendix C

On basis of consolidation with Denver & Salt Lake

		First Mtg. Bonds						Income Bonds				
	Claims as of Jan. 1, 1942	Formula Distribution	Distribution of R. F. C. excess of 2,395,841	New Allocation	Final	Formula Distribution	Deduct for foregoing increase in first mtg. bonds	New Allocation	Final	Pref. Stock	Com. Stock
R. G. Western first-trust 4's	$19,448,200	66% $12,832,512	Earnings $866,100 43.2%	$1,035,003	$13,867,515	71% $13,804,672	34% $6,610,688	$1,035,003	$5,575,685	29% $5,638,528		
R. G. Western consol. 4's	19,453,200					6% 1,167,192	—		1,167,192	6% 1,167,192	69% $13,422,708	25% $4,863,300
Junction first-trust 5's	2,658,333	66% 1,754,500	126,362 6.3%	150,938	1,905,438	71% 1,887,416	34% 903,833	150,938	752,895	29% 770,917		
D. & R. G. consol. 4's	44,362,500	21% 9,316,125		757,450	10,073,575	23% 10,203,375	13% 6,876,795	903,232	5,973,563	11% 4,879,875	22% 9,759,750	44% 19,519,500
D. & R. G. consol. 4½'s	8,535,925	21% 1,792,544	754,095 37.7%	145,782	1,938,326	23% 1,963,263				11% 938,952	22% 1,877,903	44% 3,755,807
Ref. and Imp't. 5's	16,350,000	16% 2,616,000		260,882	2,876,882	18% 2,943,000	10% 1,922,000	306,668	1,615,332	8% 1,308,000	21% 3,433,500	53% 8,665,500
Ref. and Imp't. 6's	2,870,000	16% 459,200	256,800 12.8%	45,785	504,986	18% 516,600				8% 229,600	21% 602,700	53% 1,521,100
			100.0%	$2,395,841								
General Mtg. 5's	42,057,755							$2,395,841				5% 2,102,888
R. F. C. Claim	13,377,209	7,197,881		7,197,881 4,802,040	4,802,040	36% 4,802,040	4,587,727	2,395,841		52% 6,983,568	12% 1,591,601	
				$2,395,841								
		$35,968,762			$35,968,762	$36,120,366	$22,068,235			$21,916,632	$30,688,162	$40,428,095
										D. & S. L.	411,100	
											$31,099,262	

IN THE

Supreme Court of the United States

October Term, 1945

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 2906 below]

SAME

vs.

THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 2907 below]

SAME

vs.

CITY BANK FARMERS TRUST COMPANY, TRUSTEE, ET ALS.,

Respondents.

[Number 3106 below]

SAME

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 3107 below]

SAME

vs.

GUY A. THOMPSON, TRUSTEE, ET ALS.,

Respondents.

[Number 3108 below]

Stipulation as to Printing of Record for Petition for Certiorari

Stipulation As To Printing of Record for Petition for Certiorari

In the first two of the above-entitled cases (Numbers 2906-2907 below, hereinafter called the Approval Appeals) the Circuit Court of Appeals for the Tenth Circuit entered an order on June 19, 1944 providing that (a) the Approval Appeals should be heard without any printed record and (b) in addition to the lengthy transcript of record certified to the Clerk of the Circuit Court by the Clerk of the District Court for the District of Colorado, there be delivered to the Circuit Court, for its use as a part of the record on the Approval Appeals, (*i*) the 10,314 pages of the printed proceedings in the District Court ("In the Matter of The Denver and Rio Grande Western Railroad Company, Debtor, In Proceedings for the Reorganization of a Railroad, No. 8669") and (*ii*) the annual reports to stockholders for the years 1936 to 1941, both inclusive, of The Denver and Rio Grande Western Railroad Company (hereinafter called the Rio Grande) and of The Denver and Salt Lake Railway Company (hereinafter called the Salt Lake). The Circuit Court entered a further order in the Approval Appeals on February 12, 1945 providing that the record therein should include the record in the last three of the above-entitled cases (Numbers 3106, 3107 and 3108 below, hereinafter called the Confirmation Appeals).

In the Confirmation Appeals an order was entered by the Circuit Court on January 17, 1945 providing that (a) the printing of the record on appeal be dispensed with and the Confirmation Appeals be heard without any printed record, (b) the record in the Confirmation Appeals should include (*i*) the record in the Approval Appeals and (*ii*) the annual reports of the Rio Grande for the years 1935, 1942 and 1943, and (c) in addition to the lengthy transcript of record certified to the Clerk of the Circuit Court by the Clerk of the

District Court, there be delivered to the Circuit Court, for its use as a part of the record on said appeals, (*i*) the "Income Account, Statement of Revenues and Expenses, Operating Performance and Statistics, Month of December, 1944," of the Rio Grande, (*ii*) the "Income Account and Financial Exhibit for the Period Ended December 31, 1944" of the Rio Grande, (*iii*) the annual report to stockholders for the year 1943 of the Salt Lake and (*iv*) the "Income, Profit and Loss and General Balance Sheet, December 31, 1944" of the Salt Lake.

All said appeals were heard in the Circuit Court without any printed record except for the documents, referred to above, that were already otherwise available in printed form. A decree was entered by the Circuit Court in all said appeals on May 10, 1945.

The parties hereinabove named as Petitioners are filing a petition (hereinafter called the Petition) for writs of certiorari to the Circuit Court to review that decree.

The persons whose names are signed hereto by counsel (hereinafter sometimes called the undersigned) are all the persons interested in the Petition. The undersigned are hereinafter sometimes referred to as (*i*) the Interests of Group 1, being the six parties hereinabove named as Petitioners; (*ii*) the Interests of Group 2, being all the appellants in the Circuit Court, namely, The Denver and Rio Grande Western Railroad Company (appellant in No. 2906 below and in No. 3107 below), The Denver and Salt Lake Western Railroad Company (appellant in No. 2907 below and in No. 3107 below), City Bank Farmers Trust Company as Trustee (appellant in No. 3106 below) and Guy A. Thompson, Trustee (appellant in No. 3108 below); (*iii*) Interests of Group 3, being all the other persons in behalf of whom appearances were entered in the Circuit Court (though none of the Interests of Group 3 otherwise participated in the

proceedings in the Circuit Court); and (*iv*) Interests of Group 4, being all the other persons* named as appellees in the notices of appeal filed in the District Court in any of said appeals, or in the titles of any of said appeals in the Circuit Court (though none of the Interests of Group 4 appeared or participated in the Circuit Court). None of the other persons who participated before the District Court or the Commission was named as an appellee, or appeared, or participated in the proceedings in the Circuit Court.

All of said material constituting the record in all of said appeals in the Circuit Court has, together with a transcript of the proceedings in the Circuit Court, been delivered to the Clerk of the Supreme Court. The undersigned desire to stipulate in accordance with paragraph 8 of Rule 38 of the Supreme Court to omit from the printed record all matter not essential to a consideration of the questions presented by the Petition.

NOW, THEREFORE, subject to the approval of the Supreme Court, the undersigned hereby stipulate and agree that:

1. For the purpose of the Petition, but not of any subsequent proceedings in the Supreme Court if the Petition be granted, the printed record shall consist of the following and only the following:

(a) The pamphlet entitled "Submission of Plan of Reorganization Pursuant to Section 77 of the Bankruptcy Act, as Amended," introduced at the hearing before the District Court on August 30, 1944 (Circuit

*Except "The First National Bank of New York" which was, by error, named as appellee in the notice of appeal by Guy A. Thompson, Trustee.

Court's Transcript in the Confirmation Appeals, p. 93, D. Ct. Transcript p. 119).

(b) "Memorandum" of the District Court dated November 1, 1944, confirming the Plan (Circuit Court's Transcript in the Confirmation Appeals, beginning at p. 433 of volume II).

(c) Order of the District Court dated November 29, 1944, confirming the Plan (Circuit Court's Transcript in the Confirmation Appeals, beginning at p. 473 of volume II).

(d) Opinion and concurring opinion in the Circuit Court dated May 10, 1945, disapproving the orders of the District Court (Transcript of Proceedings in the Circuit Court at pp. 601-626).

(e) Order of the Circuit Court dated May 10, 1945 reversing the orders of the District Court (Transcript of Proceedings in the Circuit Court at p. 627).

(f) The oral opinion of the District Court delivered on September 14, 1943 appearing at pages 144-146 of volume I of the transcript before the Circuit Court in the Confirmation Appeals (pages 181-183 of the District Court transcript).

(g) Order number 484 of the District Court beginning at page 1828 of volume 3 of the transcript before the Circuit Court in the Approval Appeals.

(h) Certificate of Interstate Commerce Commission dated July 4, 1944 concerning results of submission of Plan to creditors, beginning at page 158 of volume I of the transcript before the Circuit Court in the Confirmation Appeals.

(i) That portion of the transcript of the hearing before the District Court on August 30-31, 1944 beginning with the word "In" in line 1 of page 1 of the copy before the Circuit Court in the Confirmation Appeals and continuing through the word "doing." on page 96, being all of the Circuit Court record of the testimony at such hearing, appearing at pages 192-288 of volume II of the transcript before the Circuit Court in the Confirmation Appeals.

(j) The following exhibits (or portion thereof) introduced at the hearing referred to in (i) above and appearing at the following pages of volume II of the transcript before the Circuit Court in the Confirmation Appeals: (*i*) only the first table (entitled "Interest on Unfunded Debt") on page 32 of the 1943 Annual Report introduced as City Bank Farmers Trust Company Ex. 8 beginning at page 353 and appearing at page 385; (*ii*) City Bank Farmers Trust Company Ex. 10 appearing at page 396; and (*iii*) City Bank Farmers Trust Company Ex. 11 appearing at page 397;

(k) The order of the District Court entered on November 29, 1944 denying the petition of City Bank Farmers Trust Company, Trustee, appearing at page 483 of volume II of the transcript before the Circuit Court in the Confirmation Appeals.

(l) The following tables attached as exhibits to the reports of the Interstate Commerce Commission and appearing at the following pages of volume 2 of the transcript before the Circuit Court in the Approval Appeals: (*i*) Exhibit A to the report of July 11, 1939 appearing between pages 1308 and 1309 (printed proceedings in the District Court, between pages 5168 and 5169); and (*ii*) Appendices A, B and C to the report of

July 13, 1942 appearing on pages 1667-1670 (printed proceedings in the District Court pages 9203-6).

(m) This Stipulation.

2. For the purposes of the printed record referred to in 1. above, the pamphlet referred to in 1.(a) and this Stipulation need not be reprinted but for the convenience of the Supreme Court Petitioners may deliver to the Clerk 40 or more copies thereof in their original ptinted form, to be bound with the other papers designated in 1. above when printed.

3. All the undersigned reserve the right to refer to any portion of the record certified from the Circuit Court to the Clerk of the Supreme Court.

4. In the event that the Petition be granted, the printed record for further proceedings thereon in the Supreme Court shall consist of (*i*) the printed record referred to in 1. above (as Volume I), and (*ii*) such portions of the entire record certified by the Circuit Court to the Clerk of the Supreme Court as the respective Interests of Groups 1 and 2 may designate for such purpose.

5. For the purpose of any other petition or petitions for certiorari that may be filed by any of the undersigned, but not of any subsequent proceedings in the Supreme Court in relation to any such other petition if granted, the printed record shall be the printed record prepared pursuant to 1. above and such printed record may be used by, and shall be deemed to have been filed by, any of the undersigned filing such other petition. In the event that any such other petition be granted, the printed record for further proceedings thereon in the Supreme Court shall consist of (*i*) the printed record prepared pursuant to 1. above (as Volume

I), and (*ii*) such portions of the entire record certified by the Circuit Court to the Clerk of the Supreme Court as the respective Interests of Groups 1 and 2 may designate for such purpose.

6. Service of the printed record, the Petition and any other petition for certiorari that may be filed, all briefs and all notices, both in connection with the Petition and any such other petition and in connection with subsequent proceedings in the Supreme Court if the Petition or any such other petition be granted, is hereby waived with respect to all Interests of Groups 3 and 4 except that one copy of each such paper shall be served on counsel for the Debtor Trustees of the Rio Grande.

7. This Stipulation may be executed in any number of counterparts, all of which together shall constitute but one instrument. The signatures hereto need not be on the same counterpart, but each signature, or any number of signatures, may be on different counterparts, or may be on separate signature sheets to be annexed to the text hereof. Execution hereof by the Interests of Groups 3 and 4 shall not impair the liberty of any of said persons, or of any other persons, to claim that they are, or are not, parties to the proceedings in the Supreme Court.

Dated as of July 16, 1945.

Interests of Group 1

Signatures of Counsel	Addresses
Hugh B. Cox HUGH B. COX *Acting Solicitor General of the United States*	Washington, D. C.
and	
W. Meade Fletcher, Jr. W. MEADE FLETCHER, JR. *Chief Railroad Counsel, Reconstruction Finance Corporation* *For Reconstruction Finance Corporation*	811 Vermont Ave., N. W. Washington 25, D. C.
Henry W. Anderson HENRY W. ANDERSON	Electric Building Richmond 12, Va.
and	
George D. Gibson GEORGE D. GIBSON. *For Insurance Group Committee*	Electric Building Richmond 12, Va.
Alexander M. Lewis ALEXANDER M. LEWIS *For Central Hanover Bank and Trust Company, Trustee*	70 Broadway New York 4, N. Y.
Edwin S. S. Sunderland EDWIN S. S. SUNDERLAND	15 Broad Street New York 5, N. Y.
and	

James L. Homire — 15 Broad Street, New York 5, N. Y.

JAMES L. HOMIRE
For Guaranty Trust Company of New York, Trustee

W. A. W. Stewart — 45 Wall Street, New York 5, N.Y.

W. A. W. STEWART
For United States Trust Company of New York, Trustee

Arthur A. Gammell — 15 Broad Street, New York 5, N.Y.

ARTHUR A. GAMMELL
For The Chase National Bank of the City of New York, Trustee

Interests of Group 2

William V. Hodges — Equitable Building, Denver 2, Colorado

WILLIAM V. HODGES

and

F. C. Nicodemus — 40 Wall Street, New York 5, N. Y.

F. C. NICODEMUS
For (i) The Denver and Rio Grande Western Railroad Company, and
(ii) The Denver and Salt Lake Western Railroad Company

Edward E. Watts, Jr.	20 Exchange Place New York 5, N. Y.
EDWARD E. WATTS, JR.	
and	
Milton J. Keegan	First National Bank Denver 2, Colorado
MILTON J. KEEGAN *For City Bank Farmers Trust Company, Trustee*	
H. H. Larimore	Missouri Pacific Bldg. St. Louis 3, Missouri
H. H. LARIMORE *For Guy A. Thompson, Trustee of Missouri Pacific Railroad Company*	

Interests of Group 3

Henry McAllister	Equitable Building Denver 2, Colorado
HENRY McALLISTER *For Wilson McCarthy and Henry Swan, as Trustees of The Denver and Rio Grande Western Railroad Company*	
Erskine R. Myer	Midland Savings Bldg. Denver 2, Colorado
ERSKINE R. MYER *For (i) H. Allyn Hicks, Jr., Trustee of The Denver and Salt Lake Western Railroad Company;* *(ii) Moffat Tunnel Improvement District, and* *(iii) Moffat Tunnel Commission*	
Paul D. Miller	20 Pine Street New York 5, N. Y.
PAUL D. MILLER *For The Chase National Bank of the City of New York*	

Interests of Group 4

H. Lawrence Hinkley	State Capitol Bldg. Denver, Colorado
H. LAWRENCE HINKLEY *Attorney General* *For (i) State of Colorado; and* *(ii) Public Utilities Commission of Colorado*	
Jesse E. Waid	14 Wall Street New York 5, N. Y.
JESSE E. WAID *For Bankers Trust Company, Trustee*	
S. Arthur Henry	Colorado Nat'l. Bank Bldg. Denver 2, Colorado
S. ARTHUR HENRY *For General Securities Company*	
Harry Hoffman	30 Pine Street New York 5, N. Y.
HARRY HOFFMAN *For Untermyer Family Group*	

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Vol. II
TRANSCRIPT OF RECORD

(Pages 369 to 896)

Supreme Court of the United States

OCTOBER TERM, 1945

No. 278

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.

No. 279

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY, ET AL.

No. 280

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

CITY BANK FARMERS TRUST COMPANY, TRUSTEE, ET AL.

No. 281

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.

No. 282

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

GUY A. THOMPSON, TRUSTEE, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

PETITION FOR CERTIORARI FILED JULY 30, 1945.

CERTIORARI GRANTED OCTOBER 8, 1945.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 278

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

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ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

VOL. II

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[fol. 369] IN THE DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF COLORADO

No. 8669

In the Matter of THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, Debtor

PETITION

To the Honorable the Judges of the District Court of the United States for the District of Colorado:

The petition of The Denver and Rio Grande Western Railroad Company, a railroad corporation organized and existing under the laws of the State of Delaware, hereinafter referred to as the "Debtor", respectfully represents:

First. That the Debtor is a railroad corporation duly organized and existing under the laws of the State of Delaware, and a citizen and resident of said State of Delaware; and is a common carrier by railroad engaged in the transportation of persons and property in interstate commerce in the States of Colorado, Utah and New Mexico, [fol. 370] and owning and operating such railroad in said states, and is not a street, suburban or interurban electric railway; and that during the six months' period immediately preceding the filing of this petition the Debtor has had, and now has, its principal executive and operating office in the City of Denver, Colorado, in the District of Colorado.

Second. That the Debtor attaches hereto as "Exhibit A" and makes a part hereof, a statement of certain of its debts now due and payable, or presently and up to and including January 1, 1936, to become due and payable.

That the Debtor is without funds to pay and discharge said obligations set forth in Exhibit A hereto, as they mature and on information and belief alleges that it has no means of borrowing or otherwise procuring funds for such purposes; that it is unable to meet its debts as they mature and it desires to effect a plan of reorganization pursuant to Section 77, of Chapter VIII of the Acts of Congress relating to bankruptcy, and especially as amended by an Act entitled "An Act To amend an Act entitled 'An Act to establish a uniform system of bankruptcy throughout the United States', approved July 1, 1898, and Acts amendatory thereof and supplementary thereto"; approved August 27, 1935.

Third. That a copy of this petition is being filed with the Interstate Commerce Commission concurrently with the filing of this petition in this court.

Fourth. That the filing of this petition by the Debtor [fols. 371-372] was duly authorized by a resolution of its Board of Directors adopted at a meeting thereof duly held on the 30th day of October, 1935.

Wherefore, your petitioner prays that an order may be entered approving this petition as properly filed under said Section 77, and that it be granted all other and further relief to which it may be entitled.

The Denver and Rio Grande Western Railroad Company, By J. S. Pyeatt, Its President.

Henry McAllister, 420 Equitable Building, Denver, Colorado. Pierce & Greer, 35 Wall Street, New York City, New York, Attorneys for Debtor.

Duly sworn to by J. S. Pyeatt, jurat omitted in printing.

[fol. 373] EXHIBIT "A"

To

Petition of the Denver and Rio Grande Western Railroad Company (The Debtor)

Statement of certain of its debts now due and payable, or presently and up to and including January 1, 1936, to become due and payable showing the character of the obligations, their respective due dates and amounts (approximate)

Due Date	Character of Obligations	Amount
	Overdue Interest on Funded Debt	
Aug. 1, 1933	Balance due coupon account for Interest on Denver & Rio Grande Western Railroad Co. 5% General Mortgage Bonds	$120,200
Jan. 1, 1935	Interest on Rio Grande Western Railway Co. First Trust Mortgage 4% Bonds	56,500
" "	Interest on Denver & Rio Grande Railroad Co. Consolidated Mortgage 4 and 4½% Bonds	826,095
April 1, 1935	Interest on Rio Grande Western Railway Co. Consolidated Mortgage 4% Bonds	301,600
" "	Interest on Denver & Rio Grande Western Railroad Co. Refunding & Improvement Mortgage 5 and 6% Bonds	360,000
July 1, 1935	Interest on Denver and Rio Grande Railroad Co. 1st Consolidated Mortgage 4 and 4½% Bonds	826,095
" "	Interest on Rio Grande Western Railway Co. 1st Trust Mortgage 4% Bonds	303,800
Aug. 1, 1935	Interest on Denver & Rio Grande Western Railroad Co. General Mortgage 5% Bonds	745,200
Oct. 1, 1935	Interest on Rio Grande Western Railway Co. 1st Consolidated Mortgage 4% Bonds	301,600
" " "	Interest on Denver & Rio Grande Western Railroad Co. Refunding & Improvement Mortgage 5 and 6% Bonds	360,000
	Total Overdue Interest	$4,201,090

[fol. 374]

Interest on Funded Debt payable on or after November 1, 1935, to and including January 1, 1936		
Nov. 1, 1935	Interest on Denver & Rio Grande Western Railroad Co. Equipment Trust, Series "C," 4½'s	$16,537
Dec. 31, 1935	Interest on The Rio Grande Junction Railway Co. First Mortgage 5% Bonds (Rental leased line)	50,000
Dec. 31, 1935	Deferred interest (due 2/1/34, 8/1/34 and 2/1/35) on Denver & Rio Western Railroad Co. General Mortgage 5% Bonds (extended by agreement)	1,863,000
Jan. 1, 1936	Interest on Denver & Rio Grande Railroad Co Consolidated Mortgage 4 and 4½% Bonds	826,095
" "	Interest on Rio Grande Western Railway Co. 1st Trust Mortgage 4% Bonds	303,800
	Total interest payable November 1, 1935—January 1, 1936	$3,059,432
Principal of notes or funded debt or sinking fund payment now due or to become due by January 1, 1936		
Mar. 31, 1934	Note payable to Railroad Credit Corporation, dated June 1, 1932	$382,646
Mar. 29, 1935	Three notes payable to Reconstruction Finance Corporation	2,000,000
On Demand	Notes payable to Reconstruction Finance Corporation, dated April 25, and June 30, 1933	1,950,000
On Demand	Note held by Reconstruction Finance Corporation, account purchase D. & S. L. Ry. stock	3,110,850
On Demand	Note payable to Chase National Bank of New York	1,500,000
On Demand	Note held by Western Pacific R. R. Corp.	17,500
On Demand	Note held by Missouri Pacific R. R. Co.	17,500
Dec. 31, 1935	Sinking fund payment under Denver & Rio Grande Western Railroad Co. Refunding & Improvement Mortgage	163,000
Jan. 1, 1936	Principal of Denver & Rio Grande Railroad Co. 1st Consolidated Mortgage 4 and 4½% Bonds,	
	In hands of public $40,507,000	
	Pledged 1445000	$41,952,000
	Total Principal	$51,093,496

[fols. 375-378]

Summary

Overdue interest on funded debt	$4,201,090
Interest on same, payable November 1, 1935-January 1, 1936	3,059,432
Principal of notes and funded debt and sinking fund payment now due or to become due by January 1, 1936	51,093,496
Total	$58,354,018

Filed November 1, 1935, 4 P. M. Charles W. Bishop, Clerk.

[fols. 377-378] IN UNITED STATES DISTRICT COURT

STATEMENT OF ASSETS AND LIABILITIES OF DEBTOR AS OF CLOSE OF BUSINESS ON OCTOBER 31, 1935

Pursuant to paragraph (6) of Order No. 1, entered herein on November 1, 1935, the Debtor The Denver and Rio Grande Western Railroad Company, files herewith a statement of its assets and liabilities as of the close of business on October 31, 1935; certified as correct by the chief accounting officer of said Debtor, namely, its General Auditor.

The Denver and Rio Grande Western Railroad Company, by Henry McAllister, Its Attorney.

[fol. 379]

The Denver and Rio Grande Western Railroad Company General Balance Sheet Statement
As of October 31, 1935

Assets

		Total Book Assets	Company's Own Issues	
Investments:				
701	Investment in Road and Equipment		210,584,177 90	
702	Improvements on Leased Railway Property		559,635 63	
704	Deposits in Lieu of Mortgaged Property Sold		37,874 64	
705	Miscellaneous Physical Property		154,871 10	
706	Investments in Affiliated Companies—Pledged		14,911,368 46	
706	Investments in Affiliated Companies—Unpledged		614,524 90	
707	Other Investments		34 00	226,862,485 73
Current Assets:				
708	Cash		1,145,373 76	
711	Special Deposits		129,186 31	
712	Loans and Bills Receivable		81,240 00	
713	Traffic and Car Service Balances Receivable		162,035 84	
714	Net Balance Receivable from Agents and Conductors		115,796 13	
715	Miscellaneous Accounts Receivable		1,492,880 32	
716	Material and Supplies		2,440,179 97	
717	Interest and Dividends		48,943 88	
718	Rents Receivable		114,029 92	
719	Other Current Assets		6,510 61	5,736,176 74

[fol. 380]

Deferred Assets:				
720 Working Fund Advances			8,464.30	
722 Other Deferred Assets			161,407.84	169,872.14
Unadjusted Debits:				
723 Rents and Insurance Premiums Paid in Advance			9,355.28	
727 Other Unadjusted Debits			7,182,321.38	7,191,676.66
729 Securities Issued or Assumed—				
Pledged (Held for Incineration)	8,333,000.00	8,333,000.00		
Pledged (Held as Collateral)	13,331,000.00	13,331,000.00		
	21,664,000.00	21,664,000.00		239,900,211.27

Liabilities

	Book Liability	Portion held by or for Company		
Stock:				
751 Capital Stock:				
Common	62,457,539.62		62,457,539.62	
Preferred	16,430,000.00		16,430,000.00	
752 Stock Liability for Conversion	15,600.00		15,600.00	
Total	78,903,139.62		78,903,139.62	
Long Term Debt:				
755 Funded Debt Unmatured	135,872,000.00	13,331,000.00	122,541,000.00	
Total Capital Liabilities	214,775,139.62	13,331,000.00	201,444,139.62	201,444,139.62
754 Grants in Aid of Construction				800,312.79

[fol. 381]

Current Liabilities:			
758 Loans and Bills Payable		6,975,714.69	
759 Traffic and Car Service Balances Payable		721,496.47	
760 Audited Accounts and Wages Payable		7,047,348.12	
761 Miscellaneous Accounts Payable		17,385.86	
762 Interest Matured Unpaid		6,180,705.00	
764 Funded Debt Matured Unpaid	8,333,000.00	3,000.00	
766 Unmatured Interest Accrued		1,397,610.23	
767 Unmatured Rents Accrued		242,574.62	
768 Other Current Liabilities		24,910.35	22,610,745.34
Deferred Liabilities:			
770 Other Deferred Liabilities			358,127.34
Unadjusted Credits:			
771 Tax Liability		951,636.31	
776 Accrued Depreciation—Equipment		9,937,985.49	
778 Other Unadjusted Credits		1,711,460.86	12,601,082.66
Corporate Surplus:			
779 Additions to Property thru Income and Surplus		407,136.88	
784 Profit and Loss		1,738,666.64	
Total Corporate Surplus			2,145,803.52
			239,960,211.27

Certified as correct, this 23rd day of December, 1935.

J. F. Morris,
General Auditor, The Denver and Rio Grande Western Railroad Company.

Field Dec. 23, 1935, 11:15 A. M. Charles W. Bishop, Clerk.

[fol. 382] IN UNITED STATES DISTRICT COURT

PETITION FOR INTERVENTION AND FOR IMPOUNDING OF INCOME OF THE DEBTOR RAILROAD COMPANY, BY CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE UNDER THE GENERAL MORTGAGE DATED FEBRUARY 1, 1924, OF THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY.

To the Honorable the Judges of the District Court of the United States for the District of Colorado:

The petition of City Bank Farmers Trust Company, as trustee under the mortgage and deed of trust of The Denver and Rio Grande Western Railroad Company, dated as of [fol. 383] February 1, 1924, respectfully shows as follows:

1. The petitioner, City Bank Farmers Trust Company, at all times hereinafter mentioned was, and still is, a corporation duly organized and existing under the laws of the State of New York and a citizen of said state having its principal office and residence in the City, County and State of New York and the Southern District of New York, and as such corporation at all times hereinafter mentioned was, and still is, duly authorized and empowered to hold in trust the property conveyed, transferred and assigned to it upon the trusts hereinafter stated, and to execute and perform the trusts reposed in it under and by virtue of the mortgage and deed of trust, dated as of February 1, 1924, (hereinafter called the "General Mortgage").

2. Upon information and belief, the debtor, The Denver and Rio Grande Western Railroad Company (hereinafter called the "Railroad Company"), is a corporation duly organized and existing under the laws of the State of Delaware and is a citizen and resident of said state, and owns or leases and, prior to the filing of its petition in this Court under Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, as hereinafter shown, operated as a common carrier by railroad, lines of railroad, substantially all continuous and connecting; and forming a complete railroad system lying within the States of Colorado, Utah and New Mexico; and its principal executive and [fol. 384] operating office is in the City of Denver, Colorado, in the District of Colorado.

3. Upon information and belief, the Railroad Company, in pursuance of resolutions adopted by the affirmative vote of more than two-thirds of its entire Board of Directors, and of resolutions adopted by the affirmative vote of the holders of its entire capital stock outstanding, at meetings duly called and held in accordance with law and with the by-laws of the Railroad Company, determined, for the purposes set forth in the General Mortgage hereinabove and hereafter referred to, to create and issue, in the manner and form as provided by such General Mortgage, its Bonds limited to an aggregate principal amount of Twenty-nine million eight hundred eight thousand dollars ($29,808,000), at any one time outstanding, to be known as the General Mortgage Sinking Fund Gold Bonds of the Railroad Company (hereinafter called the "Bonds").

4. Upon information and belief, the Railroad Company, in pursuance of resolutions adopted by the affirmative vote of more than two-thirds of its entire Board of Directors, and of resolutions adopted by the affirmative vote of the holders of its entire capital stock outstanding, at meetings duly called and held in accordance with law and with the by-laws of the Railroad Company, in order to secure the payment of all the Bonds at any time issued and outstanding under such General Mortgage, according to their tenor, purport and effect, as well the interest as the principal [fol. 385] thereof, and to secure the performance and observance of all the covenants and conditions therein and in said General Mortgage contained, and to declare the terms and conditions upon which the Bonds were to be issued, determined to and did duly make, and on or about December 20, 1924, execute under its corporate seal and deliver to the petitioner, City Bank Farmers Trust Company, as trustee, a mortgage and deed of trust dated as of February 1, 1924. The petitioner prays leave to refer to the General Mortgage, or to a copy thereof when the same shall be produced upon the final hearing, or upon any hearing in this proceeding, with the same force and effect as if said General Mortgage were herein set forth at length.

5. In and by the General Mortgage, the Railroad Company, for the purposes and on the conditions therein set forth, granted, bargained, sold, aliened, remised, released, conveyed, confirmed, assigned, transferred and set over unto the trustee, its successors in the trust and its and their as-

[fol. 395] each and all of said Bonds and Scrip Certificates were duly delivered to the Railroad Company or upon its order pursuant to the terms of the General Mortgage. Upon information and belief all of said Bonds and Scrip Certificates therefor were duly issued and, with their appurtenant unpaid coupons, now are outstanding and now are the lawfully created, valid and existing obligations of the Railroad Company and entitled to the lien and security of the General Mortgage and are in the hands of numerous bona fide holders for value.

15. Section 3 of Article Nine of the General Mortgage provides, among other things, as follows (the "Railroad Company" therein mentioned being the debtor Railroad Company, the "indenture" therein mentioned being the General Mortgage, and the "Trustee" therein mentioned being the petitioner):

"Section 3. Unless and until

"A. * * * ; or

"B. there shall be a default in the payment of some installment of interest on some General Mortgage Bond at the time outstanding; or

"C. some one of the events of default specified in subdivisions (b), (c), (d), (e), (f), (g) or (h) of Section 2 of Article Ten hereof shall happen:

(a) the Trustee shall not (except with the assent of the Railroad Company or as otherwise author- [fol. 396]- ized by this indenture), whether at, or before, or after the maturity thereof, be entitled to enforce the collection of, the principal or interest of any bonds or obligations or of any other claims or indebtedness subject to this indenture, and shall not enforce any provisions of the mortgages, trust deeds or other instruments under which such bonds or other obligations were issued, or by which the same are secured; * * *."

The General Mortgage, in Article Ten thereof, provides, among other things, as follows (the "Railroad Company" therein mentioned being the debtor Railroad Company, the

"indenture" therein mentioned being the General Mortgage, and the "Trustee" therein mentioned being the petitioner):

"Section 2. If one or more of the following events, in this indenture called events of default, shall happen, that is to say:

(a) default shall be made in the payment of any instalment of interest on any of the General Mortgage Bonds when and as the same shall become payable, as therein and herein expressed, and such default shall continue for ninety days; or"

* * * * * * *

(c) default shall be made in the payment of any instalment of the sinking fund created for the General Mortgage Bonds by Article Five hereof, [fol. 397] and such default shall continue for one hundred and twenty days; or

(d) default shall be made in the observance or performance of any other of the covenants, conditions and agreements on the part of the Railroad Company, its successors or assigns, in the General Mortgage Bonds or in this indenture contained, and such default shall continue for one hundred and twenty days after written notice specifying such default and requiring the same to be remedied shall have been given by the Trustee, which shall give such notice, on the written request of the holders of twenty per cent in principal amount of the General Mortgage Bonds at the time outstanding; or

(e) an order shall be ~~made for~~ the appointment pendente lite of a receiver (but not a temporary receiver) of the Railroad Company or of the trust estate substantially as a whole; or

(f) default shall be made in the payment of the interest on any bond or obligation secured by direct lien prior to that of this indenture on the mortgaged lines of railway or any part thereof and such default shall continue for the period of grace, if any, specified in the mortgage or other instrument securing such bond or obligation; or

signs, all the right, title and interest of the Railroad Company in and to all and singular the lines of railroad, and all property and rights held for use in connection therewith, or appertaining thereto, extensions, additions, improvements and betterments, other properties and franchises, shares of capital stock and bonds, "all tolls, revenues, earnings, income, rents, issues and profits of the railways, premises and property and every part thereof" described therein. In the General Mortgage it was provided that the properties [fol. 386] were assigned and conveyed subject to certain liens therein more particularly described.

6. In addition to the property described in the granting clauses of the General Mortgage, provision is made in Article Seven thereof with respect to stock of the Utah Fuel Company as follows (the "Railroad Company" therein mentioned being the debtor Railroad Company, "indenture" therein mentioned being the General Mortgage, the "Trustee" therein mentioned being the petitioner and the "Refunding and Improvement Mortgage" therein mentioned being a certain mortgage and deed of trust executed by the Railroad Company, dated as of February 1, 1924 and constituting a lien on the property therein described prior to that of the General Mortgage):

"Section 1. Simultaneously with the execution hereof there has been executed an agreement between the Railroad Company, Missouri Pacific Railroad Company, The Western Pacific Railroad Corporation and James S. Alexander, Trustee, relating to the stock of Utah Fuel Company, (hereinafter sometimes called the Utah Fuel Agreement), and an assignment of its rights and interests under said agreement by the Railroad Company to the trustee under the Refunding and Improvement Mortgage, and, subject thereto, to the Trustee hereunder. By the Utah Fuel Agreement and the assignment thereof it is, among other things, [fol. 387] provided that in the event of the foreclosure or enforcement hereof pursuant to the provisions of Article Ten hereof, the Trustee hereunder, or the Preferred Stockholders Committee in said agreement referred to, shall have the power to require the sale by the trustee under said agreement of the stock of Utah Fuel Company, the subject of said agreement (or any securities or other property held subject to said agree-

ment for which such stock may have been exchanged pursuant to the terms of said agreement) and the application of the proceeds to the payment of the Refunding Bonds and thereafter the bonds issued hereunder in the same manner as if such stock (or substituted securities or property as in said agreement provided) had been pledged under the Refunding and Improvement Mortgage and subject thereto, hereunder, (subject to the existing charge, if any, upon said stock in favor of the First Consolidated Mortgage 4% Fifty Year Gold Bonds of The Rio Grande Western Railway Company, secured by the First Consolidated Mortgage Deed of said Railway Company to The State Trust Company, Trustee [Guaranty Trust Company, of New York, successor trustee], herein sometimes called the First Consolidated Mortgage, dated April 1, 1899, and any indentures supplemental thereto) and if the Trustee hereunder or said Preferred Stockholders Committee shall so request, before the application to the payment of the Refunding Bonds or the bonds [fol. 388] issued hereunder, of the properties subject to this indenture, or the proceeds thereof.

"In the event that said stock (or substituted securities or other property), shall be so sold at the instance of the trustee under the Refunding and Improvement Mortgage or the Trustee hereunder or said Preferred Stockholders Committee, and the proceeds thereof shall be subject to be applied in whole or in part to the payment of the bonds issued hereunder and/or the interest accrued thereon, either under the direction of any court having jurisdiction of the foreclosure or enforcement of this indenture or otherwise, said proceeds shall be applied to the payment of said bonds and/or the interest thereon in the same manner, in the same order of priority and with the same effect as if said stock or substituted securities or other property until the sale thereof at all times had been a part of the securities subject hereto and had been so sold."

The petitioner prays leave to refer to said Utah Fuel Agreement and to said assignment, or to copies thereof when the same shall be produced upon the final hearing, or upon any hearing in this proceeding, with the same force

and effect as if said Utah Fuel Agreement and said assignment were herein set forth at length.

7. In addition to the provisions with respect thereto found in the granting clauses of the General Mortgage, the [fol. 389] tolls, revenues, earnings, income, rents, issues and profits of the mortgaged property were specifically and primarily pledged in Section 1 of Article Fifteen to the payment of the principal and interest of the Bonds, as follows (the "Railroad Company" therein mentioned being the debtor Railroad Company, the "indenture" therein mentioned being the General Mortgage, and the "Trustee" therein mentioned being the petitioner):

"Section 1. Until some default shall have been made in the due and punctual payment of the interest or of the principal of the General Mortgage Bonds at any time outstanding, or of some part of such interest or principal, or until some one or more of the events of default specified in clauses (c), (d), (e), (f), (g) and (h) of Section 2 of Article Ten hereof shall have happened, the Railroad Company, its successors and assigns, shall be suffered and permitted to retain actual possession of all the property subject to this indenture (other than bonds, certificates of stock, cash and other property assigned or pledged, or to be assigned or pledged, hereunder), and to manage, operate and use the same and every part thereof, with the rights and franchises appertaining thereto, and to collect, receive, take, use and enjoy the tolls, earnings, income, rents, issues and profits of such property (as well as of such stock, bonds, cash and other property so assigned or pledged).

"The Railroad Company covenants and agrees that from such income, after payment of the operating and [fol. 390] maintenance expenses of the mortgaged premises embraced in the trust estate, taxes and other proper prior charges, the interest maturing upon the General Mortgage Bonds, so far as such income shall not be applied to the payment of the interest maturing on other bonds or obligations secured by mortgage or other instrument prior in lien to this indenture upon the trust estate, shall, subject to the provisions of Article Six hereof, first be paid, and such income

whether before or after the happening of an event of default and whether the mortgaged premises be operated by the Railroad Company or by the Trustee under any power reserved under this indenture, or by a receiver or receivers appointed by any court at the instance of the Railroad Company or of the Trustee or of any mortgagee, stockholder, creditor or other person interested in the Railroad Company and having the right to apply for such appointment, shall be primarily pledged and applied, subject only as otherwise in this indenture specifically provided, to the payment of the principal and interest of the General Mortgage Bonds."

8. It is provided in the General Mortgage that all of the properties assigned and conveyed to the petitioner were so assigned and conveyed for the common and equal use, benefit and security of all and singular the person or persons, firm or firms, bodies politic or corporate, who should from time [fol. 391] to time be holders of any of the Bonds or coupons and without preference of any of said Bonds over any other or others of said Bonds by reason of priority in the time of issue or negotiation thereof or otherwise howsoever.

9. Section 14 of Article Eight of the General Mortgage provides as follows (the "Railroad Company" therein mentioned being the debtor Railroad Company, "indenture" therein mentioned being the General Mortgage, the "Trustee" therein mentioned being the petitioner and the "Refunding and Improvement Mortgage" therein mentioned being a certain mortgage and deed of trust executed by the Railroad Company, dated as of February 1, 1924 and constituting a lien on the property therein described prior to that of the General Mortgage):

"Section 14. At all times the Railroad Company will keep on its books a separate list of locomotives, tenders, cars and other equipment subject to this indenture as a direct first lien or subject to the Refunding and Improvement Mortgage as a direct first lien, and prior to January 1, 1926, it will furnish to the Trustee a complete list of all such locomotives, tenders, cars and other equipment on which this indenture or the Refundin and Improvement Mortgage shall then be a direct st lien, and thereafter it will annually prior to

every January 1, and at such additional times as the Trustee may request, furnish to the Trustee a corrected [fol. 392] list thereof, so as to enable the Trustee at all times, to identify the locomotives, tenders, cars and other equipment upon which this indenture or the Refunding and Improvement Mortgage is a direct first lien."

10. The petitioner duly accepted the trusts created by the General Mortgage and executed the same to evidence such acceptance.

11. Upon information and belief, since the date of the execution and delivery of the General Mortgage, the Railroad Company has from time to time acquired certain other property, real and personal, rights and interest (the exact character, description and extent of which are at present unknown to the petitioner), which have become subject to the lien of the General Mortgage, and for the proper protection and enforcement of the rights of the petitioner and of the holders of the Bonds and interest obligations, it is necessary for the Railroad Company and any trustees appointed under Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, to account to the petitioner in this proceeding for all property, rights and interests owned by the Railroad Company at the date of the execution and delivery of the General Mortgage, and for all property, rights and interests subsequently acquired by the Railroad Company; and for certain property released from the lien of the General Mortgage, and to exhibit in this proceeding a full and true description thereof, in order that said property, rights and interests or so much thereof as [fol. 393] is subject to the lien of the General Mortgage, may be so declared and decreed by this Court.

12. Upon information and belief, subsequent to the execution and delivery of the General Mortgage, the same was duly recorded in each county in which the lines of railroad and other property of the Railroad Company covered by the General Mortgage were and are situated or located, and elsewhere as required by law, except that the General Mortgage was not recorded in the Counties of Jefferson and Park in the State of Colorado nor in the Counties of Garfield, Duchesne and Uintah in the State of Utah where certain rights of way which had been acquired by the Rail-

road Company were not used or intended for railroad purposes.

13. Upon information and belief, the General Mortgage and the assignment of the Railroad Company's rights and interests under the Utah Fuel Agreement were and are the proper act and deed of the Railroad Company, and were by it authorized, made and delivered in all respects in conformity with law, and the same were and are valid conveyances for the purposes therein stated and now constitute valid and subsisting liens upon all the property therein mentioned and set forth and covered by or embraced in or under the General Mortgage and said assignment, or intended so to be, or which has become subject to the lien of the General Mortgage and said assignment.

[fol. 394] 14. By Article Two of the General Mortgage it is, among other things, provided that Twenty-nine million eight hundred eight thousand dollars ($29,808,000) principal amount of Bonds, should, forthwith upon the execution and delivery of the General Mortgage, or at the option of the Railroad Company at any time or from time to time thereafter, be executed by the Railroad Company and delivered by it for authentication to the petitioner, and that thereupon, as provided therein, the petitioner should authenticate and deliver the same. From time to time the petitioner, in conformity with the provisions of the General Mortgage has duly authenticated Twenty-nine million seven hundred forty-nine thousand and seven hundred dollars ($29,749,700) principal amount of Bonds in definitive form, Forty-three thousand five hundred dollars ($43,500) principal amount of Bonds in temporary form, and Fourteen thousand eight hundred dollars ($14,800) principal amount of Scrip Certificates for Bonds. Some of the foregoing Bonds were in form of coupon bonds and some were in form of registered bonds, but all of such Bonds and all of such Scrip Certificates were in the forms, respectively, provided in the General Mortgage and as prescribed, upon information and belief, in resolutions duly adopted by the Board of Directors of the Railroad Company as provided in the General Mortgage; and upon information and belief all of such Bonds and Scrip Certificates for Bonds had been theretofore duly executed by the Railroad Company pursuant to authority of law and due corporate action, and thereupon

[fol. 398] (g) the Railroad Company shall fail, on the maturity of said bonds or obligations specified in the foregoing clause (f) of this Section 2 (or if the time for the payment of the principal of any of said bonds or obligations shall have been extended pursuant to the right reserved in Section 7 of Article Eight hereof, on such extended maturity) and on presentation thereof in accordance with the terms thereof, either to pay said bonds or obligations or to cause said bonds or obligations to be taken up and delivered to the Trustee to be held under this indenture or otherwise to deal with such bonds or obligations as may be required or permitted by this indenture; or

(h) default shall be made in the performance of any covenant contained in any mortgage or deed of trust or other instrument constituting a direct lien on any part of the mortgaged lines of railway in priority to this indenture and, by reason of such default, any right of entry or right of action for the enforcement of the security afforded thereby shall accrue;

then and in each and every such case the Trustee personally, or by its agents or attorneys, while such default shall continue, may enter into and upon all or any part of the railways, rolling stock, property and premises, lands, rights, interests and franchises hereby [fol. 399] conveyed, or intended so to be, and each and every part thereof, and may exclude the Railroad Company, its agents and servants wholly therefrom; and, having and holding the same, may use, operate, manage and control said railways and other premises, regulate the tolls for the transportation of passengers and freight thereon, and conduct the business thereof, either personally or by its superintendents, managers, receivers, agents and servants or attorneys; * * *. And the Trustee shall be entitled to collect and receive all tolls, earnings, income, rents, issues and profits of the same and every part thereof, and also the income from stocks and bonds and other obligations and securities subject to this indenture."

* * * * * * *

"Section 3. If one or more of the events specified in Clauses A, B or C of Section 3 of Article Nine hereof shall happen, the Trustee shall be entitled, while such event shall continue, to vote on all shares of stock then held under this indenture, and, for the benefit of the holders of the General Mortgage Bonds, to collect and receive all dividends on all such shares of stock, and all sums payable for principal, interest or otherwise upon any bonds or obligations or other indebtedness that shall then be pledged under this indenture, and to apply, as hereinbefore in Section 2 of this Article Ten provided, the net moneys received; and, [fol. 400] as holder of any such shares of stock and of any such bonds or other obligations and such indebtedness, to perform any and all acts, or to make or execute any and all transfers, requests, requisitions or other instruments for the purpose of carrying out the provisions of this Section 3; but in the event that a receiver of the railways embraced in the trust estate shall have been appointed and shall be in possession thereof in the enforcement of this indenture or pursuant to the provisions hereof, the Trustee from time to time in its discretion may, and if requested by the holders of a majority in principal amount of the General Mortgage Bonds at the time outstanding, shall turn over any part or all of the interest moneys and dividends so collected by it to such receiver, and the Trustee may co-operate with such receiver in managing and operating the system of the Railroad Company in such manner as the Trustee shall deem for the best interest of the holders of the General Mortgage Bonds."

* * * * * * *

"Section 17. Upon filing a bill in equity, or upon commencement of any other judicial proceedings, to enforce any right of the Trustee or of the bond-holders under this indenture, the Trustee shall be entitled, as matter of right, to the appointment of a receiver of the premises and property subject to this indenture, and of any other property owned by the Railroad Com- [fol. 401] pany, used for, in or about, or the use and possession whereof is essential to, the operation of the lines of railway and railway properties subject to this indenture or any thereof, and of the earnings,

income, revenues, rents, issues and profits of the premises and property subject hereto with such powers as the court making such appointment shall confer; but notwithstanding the appointment of any receiver, the Trustee shall be entitled, as pledgee, to continue to retain possession and control of any shares of stock, bonds, cash and other property pledged or to be pledged, and held hereunder, and to retain control of any moneys deposited with other depositaries as in this indenture provided."

"Section 18. In case the Railroad Company shall make default in any of the respects mentioned in Section 2 of this Article Ten, and (1) at any time during the continuance of such default there shall be any existing judgment against the Railroad Company unsatisfied and unsecured by bond on appeal or (2) in any judicial proceeding by any party other than the Trustee, a receiver shall be appointed of the Railroad Company or of its property or any part thereof, or a judgment or order be entered for the sequestration of its property or any part thereof; or in case the Railroad Company shall make default in the payment of interest specified in subdivision (a) of said Section 2, and shall by resolution of its Board of Directors admit to the Trustee its inability to make good such de- [fol. 402] fault within the period of grace in said subdivision (a) mentioned; the Trustee, in either such case, without waiting the period of grace, if any, in said Section 2 specified in respect of such default, shall thereupon be entitled, in the discretion of the Trustee, forthwith to exercise the right of entry herein conferred, and also any and all other rights and powers herein conferred and provided to be exercised by the Trustee upon the happening of an event of default as hereinbefore provided, and as matter of right the Trustee shall thereupon be entitled, in the discretion of the Trustee, to the appointment of a receiver of the trust estate, and of the earnings, income, revenue, rents, issues and profits thereof, and of any other property of the Railroad Company used for, in or about, or the use or possession whereof shall be essential to, the operation of the lines of railway and railway properties subject hereto or any thereof, with such powers

as the court making such appointment shall confer; *provided*, however, that notwithstanding the appointment of any such receiver, the Trustee shall be entitled as pledgee, to continue to retain possession and control of any shares of stock, bonds, cash and other property pledged or to be pledged, and held hereunder, and to retain control of any moneys deposited with other depositaries as in this indenture provided."

[fol. 403] 16. Upon information and belief, heretofore and on or about November 1, 1935, the Railroad Company filed in this Court its petition as debtor under Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, which petition represented, among other things, that the Railroad Company was duly organized and existing under the laws of the State of Delaware, and a common carrier by railroad engaged in the transportation of persons and property in interstate commerce, in the States of Colorado, Utah and New Mexico; that on the date of the petition (October 30, 1935) certain of its debts were then due and payable, or presently and up to and including January 1, 1936, would become due and payable all as set forth in a statement attached to the petition of the Railroad Company; and the Railroad Company alleged upon information and belief that it would be unable to procure funds with which to pay and discharge such obligations as they became due and payable; that the Railroad Company was unable to meet its debts as they matured and desired to effect a plan of reorganization pursuant to Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, and especially as amended by an Act entitled "An Act to Amend an Act entitled 'An Act to Establish a Uniform System of Bankruptcy throughout the United States', approved July 1, 1898, and Acts Amendatory thereof and Supplementary thereto", approved August 27, 1935; that the Railroad Company was, concurrently with the filing of said petition [fol. 404] in this Court, causing to be filed with the Interstate Commerce Commission a copy of the petition; that the filing of said petition was duly authorized by a resolution of the Board of Directors of the Railroad Company adopted at a meeting thereof held on October 30, 1935. The said petition prayed that an order might be entered approving the petition as properly filed under said Section

77, and that it be granted all other and further relief to which it might be entitled.

17. Upon information and belief, upon the filing of said petition by the Railroad Company and on or about November 1, 1935, an order was made and entered by this Court, which order, among other things, directed that the petition be approved as properly filed under Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, and authorized the Railroad Company, pending further order of this Court, among other things, to run, manage, maintain, operate and keep in proper condition and repair the railroads, railroad systems and property of the Railroad Company, wherever situated, whether in the state and judicial district of Colorado, or elsewhere, and to manage and conduct its business as a railroad company, all according to law and subject to such supervision and control by the Court as the Court might exercise by its further orders entered herein.

18. The petitioner prays leave to refer to said petition of the Railroad Company, and the said order entered thereon, [fol. 405] or to duly certified copies thereof when the same shall be produced upon the final hearing, or upon any hearing in this proceeding, with the same force and effect as if said petition and order were herein set forth at length.

19. Upon information and belief, the Railroad Company, subsequent to the entry of the aforesaid order by this Court, has operated the lines of railroad, properties and premises of every kind and description, including the properties subject to the lien of the General Mortgage, and has collected and received the tolls, revenues, earnings, income, rents, issues and profits of said property and of the property subject to the Utah Fuel Agreement subject to the supervision and control of this Court pursuant to said order and to the provisions of Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, by reason whereof the petitioner is unable, save as herein sought, to take possession thereof and to administer its trust as in the General Mortgage and in the assignment of the Railroad Company's rights and interests under the Utah Fuel Agreement it is provided should be done in the event of a default as herein specified.

20. Upon information and belief, the Railroad Company has defaulted in the payment of the interest due on January 1, 1935 on $2,825,000 principal amount of The Rio Grande Western Railway Company First Trust Four Per Cent Gold Bonds due July 1, 1939 and in the payment of interest [fol. 406] due on July 1, 1935 on $15,190,000 principal amount of said The Rio Grande Western Railway Company First Trust Four Per Cent Gold Bonds due July 1, 1939, all secured by the First Trust Mortgage dated July 1, 1889 made by The Rio Grande Western Railway Company; in the payment of interest due on April 1, 1935 and October 1, 1935 on $15,080,000 principal amount of The Rio Grande Western Railway Company First Consolidated and Collateral Trust Four Per Cent Gold Bonds due April 1, 1949, secured by the First Consolidated Mortgage dated April 1, 1899 made by The Rio Grande Western Railway Company; in the payment of interest due on January 1, 1935 and July 1, 1935 on $34,125,000 principal amount of The Denver and Rio Grande Railroad Company First Consolidated Four Per Cent Gold Bonds due January 1, 1935 and in the payment of interest due on January 1, 1935 and July 1, 1935 on $6,382,000 principal amount of The Denver and Rio Grande Railroad Company First Consolidated Four and One-Half Per Cent Gold Bonds due January 1, 1936, all secured by the Consolidated Mortgage dated July 15, 1886 as supplemented January 1, 1898 made by The Denver and Rio Grande Railroad Company; in the payment of interest due on April 1, 1935 and October 1, 1935 on $2,000,000 principal amount of The Denver and Rio Grande Western Railroad Company Refunding and Improvement Six Per Cent Gold Bonds, Series A, due October 1, 1974 and in the payment of interest due on April 1, 1935 and October 1, 1935 on $12,000,000 principal amount of The Denver and [fol. 407] Rio Grande Western Railroad Company Refunding and Improvement Five Per Cent Gold Bonds, Series B, due April 1, 1978, all secured by the Refunding and Improvement Mortgage, dated as to Series A, February 1, 1924, and as to Series B, April 1, 1928, made by The Denver and Rio Grande Western Railroad Company, all of said mortgages constituting direct liens prior to that of the General Mortgage on the lines of railroad or parts thereof subject to the General Mortgage or owned by a controlled company of the Railroad Company, and such default still continues.

21. Upon information and belief, by reason of the defaults mentioned in the foregoing paragraph 20 and by reason of the fact that, as alleged hereinabove in paragraph 17 this Court in the above entitled proceeding has approved the petition of the Railroad Company as properly filed under Section 77 of Chapter VIII of the Acts of Congress relating to Bankruptcy, and authorized the Railroad Company, pending the further order of this Court, among other things, to take control of and operate the trust estate substantially as a whole, and by reason of the happening of other events of default as specified in Section 2 of Article Ten of the General Mortgage, the petitioner is entitled, under the terms of the General Mortgage, to exercise the right of entry thereby conferred and to proceed to protect and enforce its rights and the rights of the holders of the Bonds in the manner described in the General Mortgage and now is entitled to collect and to receive all tolls, reve- [fol. 408] nues, earnings, income, rents, issues and profits of the mortgaged premises, and also the income from stocks and bonds and other obligations and securities subject to the General Mortgage and to apply the same as provided in the General Mortgage, and also to exercise the right conferred by the assignment of the rights and interests of the Railroad Company under the Utah Fuel Agreement to require the sale by the trustee under said Agreement of the stock of Utah Fuel Company, the subject of said Agreement (or any securities or other property held subject to said Agreement for which such stock may have been exchanged pursuant to the terms of said Agreement) and generally to exercise any and all rights and powers in and by the General Mortgage and said assignment conferred and provided to be exercised by the petitioner thereupon, upon the occurrence and continuance of any default as in the General Mortgage provided.

22. Upon information and belief, default has been made by the Railroad Company in the payment of the installment of interest which became due on August 1, 1935 upon all of the Bonds issued and outstanding and secured by the General Mortgage and that such default still continues.

23. Upon information and belief, the Board of Directors of the Railroad Company decided at a meeting held on January 27, 1934 to withhold, for the time being, payment

of interest due February 1, 1934 on the Bonds and at a meet-
[fol. 409] ing held on March 23, 1934 proposed a plan for avoiding a default under the General Mortgage. The plan provided that holders of the Bonds who assented thereto would receive payment of one-half of the February 1, 1934 coupon and should withhold, until December 1, 1935, presentation of the balance of said coupon and the full amount of the coupons maturing August 1, 1934 and February 1, 1935. The Railroad Company placed in a special deposit subject to requisition by City Bank Farmers Trust Company, as agent for the Railroad Company, a sum sufficient to pay Fifty per cent (50%) of the face amount of the interest coupon on the Bonds of the Railroad Company due February 1, 1934. As of October 31, 1935 holders of $23,555,600 principal amount of the Bonds out of the total authorized and outstanding issue of $29,808,000 had assented to the plan by presenting to City Bank Farmers Trust Company, as agent for the Railroad Company, the three coupons due respectively, February 1, 1934, August 1, 1934 and February 1, 1935, detached from the Bonds, for endorsement of the payment of one-half of the face amount of the February 1, 1934 coupon, and for stamping each of such coupons with an appropriate legend indicating the acceptance of the plan. It was provided in the plan that whenever the Railroad Company determined that sufficient of the holders of the Bonds had accepted the plan to make the same effective, it would declare the plan operative by serving notice thereof on City Bank Farmers Trust Company and causing notice thereof to be published and thereupon pre-
[fol. 410] sentation of each of such coupons stamped, as aforesaid, should be deferred until December 31, 1935. It was further provided in the plan that in the event receivers or trustees for the Railroad Company were appointed, the holders of the Bonds and the coupons presented for stamping should cease to be subject to the plan. Upon information and belief City Bank Farmers Trust Company, in its individual or in any other capacity, has received no notice from the Railroad Company nor from any other source declaring the plan operative. Upon information and belief, holders of the Bonds who did not assent to the plan have received no payment on said coupons maturing respectively February 1, 1934, August 1, 1934 and February 1, 1935.

24. Upon information and belief, various mortgages exist upon the properties of the Railroad Company including the General Mortgage, as aforesaid; the liens and provisions of said mortgages differ among themselves and the aggregate of the outstanding Bonds secured by them, respectively, is very great, amounting to many millions of dollars; some or all of said mortgages purport, or may be claimed, to constitute liens upon the property covered by the lien of the General Mortgage, or some portions thereof, wholly or partly superior to the General Mortgage lien, but the amount and extent of such liens, if any, are unknown to your petitioner.

25. No proceedings have been had at law or in equity for the protection and enforcement of the rights of the peti- [fol. 411] tioner, and/or of the rights of the holders of the Bonds or for the foreclosure of the General Mortgage or for the collection or enforcement of the mortgage debt, or any part thereof, or for the enforcement of the rights conferred by the assignment of the rights and interests of the Railroad Company under the Utah Fuel Agreement, save only this proceeding, and the petitioner has no adequate relief at law, and the relief to which it is entitled can only be granted by this Court.

26. Upon information and belief, the Railroad Company owns or leases and operates lines of railroad, substantially all continuous and connecting and forming a complete railroad system, lying within the States of Colorado, Utah and New Mexico; the Railroad Company owns and leases certain rolling stock and equipment and owns other property, real and personal, as well as rights, privileges and franchises appertaining to, or used in connection with, its lines of railroad and business, and certain bonds, stocks and other securities. The petitioner is advised and, therefore, avers that by reason of the premises and of the matters hereinbefore in this petition alleged, and of the defaults hereinbefore in this petition alleged, as well as by reason of the impairment of and danger and injury to the security of its said mortgage lien hereinbefore alleged, the petitioner is entitled to file this petition, to have the relief herein prayed for, and to have all such tolls, revenues, earnings, income, rents, issues and profits of the properties of the Railroad Company

[fol. 412] and every part thereof segregated and sequestered for the benefit of the petitioner and of the holders of the Bonds and interest obligations secured by said mortgage lien; and the petitioner hereby demands that said tolls, revenues, earnings, income, rents, issues and profits be so segregated and sequestered as aforesaid, and be applied, subject only to such expenses and other uses as may legally and properly, having due regard to the rights of the petitioner and the holders of the Bonds, be incurred and made in the operation and preservation of the property, rights and franchises covered by the petitioner's said mortgage lien, to and for the benefit of the petitioner and of the holders of the Bonds and interest obligations, and to and for the proper protection of the petitioner's said mortgage lien and the security thereof.

27. Upon information and belief, numerous questions of vital and far-reaching importance, in so far as they affect the General Mortgage and the interests of the holders of the Bonds, will be raised in the above entitled proceedings to come before this Court for its decision thereon, and, therefore, the petitioner alleges that, in view of the importance to it and to the holders of the Bonds of the questions which will arise from time to time in these proceedings, it should be permitted to intervene in these proceedings for the purpose of protecting its rights and interests and the interests of the holders of the Bonds.

28. By reason of the premises the petitioner is unable adequately to execute its trust in the manner specified and [fol. 413] provided in and by the General Mortgage without the aid and interposition of this Court, nor can its said trust be executed, as the petitioner is advised and charges, and the rights of all the parties in interest be ascertained and fully protected, otherwise than by segregating and sequestering the tolls, revenues, earnings, income, rents, issues and profits of the Railroad Company and every part thereof.

Wherefore, the petitioner prays:

1. That the petitioner be permitted to intervene generally in the above entitled proceeding for the purpose of protect-

ing its rights as trustee under the General Mortgage, dated as of February 1, 1924, and the rights of the holders of the Bonds issued thereunder, and further and more specifically for the purposes of this petition; and that this Court direct that notices of all motions, applications and petitions herein be served upon the attorneys for the petitioner;

2. That the General Mortgage and the assignment of the rights and interests of the Railroad Company under the Utah Fuel Agreement may be decreed to be valid and subsisting liens, upon all of the railroads and property, real and personal, rights, privileges and franchises in the General Mortgage and said assignment described or thereby conveyed or transferred or intended so to be, or shall have become subject thereto (save and except such property as may have been duly released from the lien of the General Mortgage), and upon the tolls, revenues, earnings, income, [fol. 414] rents, issues and profits of the Railroad Company and every part thereof, prior and superior to the interests or liens or claims of the debtor Railroad Company;

3. That the nature, extent and character of said property and premises may be ascertained and determined; that an account be taken of all the railroads and property, real personal and mixed, which belonged to the Railroad Company at the date of the above mentioned General Mortgage and of all the railroads, property, additions, extensions, improvements, renewals and replacements acquired by the Railroad Company since the date of said General Mortgage;

4. That this Court direct the Railroad Company and such trustee or trustees, appointed in this proceeding, of the Railroad Company as may from time to time be acting, to keep such records and accounts, in addition to the accounts prescribed by the Interstate Commerce Commission, as will permit the segregation and allocation of the earnings and expenses between and to the divisions and parts of the property of the Railroad Company, which are separately subject to the liens of the several mortgages of the Railroad Company;

5. That this Court determine upon a method or formula by which such segregation and allocation shall be made,

with due regard to the rights and interests of the petitioner, as trustee under the General Mortgage and of the holders of the Bonds, and refer to the Interstate Commerce Com-
[fol. 415] mission for its recommendations after hearings thereon, if the parties to these proceedings shall so request, or if said Commission shall determine the same to be necessary or desirable, as to the method or formula by which such segregation or allocation shall be made.

6. That this Court direct that such segregation and allocation be made at the expense of the estate of the Railroad Company;

7. That all tolls, revenues, earnings, income, rents, issues and profits of the property subject to the lien of the General Mortgage, and every part thereof, which shall come into the possession of the Railroad Company or of any trustee or trustees thereof appointed in this proceeding be impounded as of the date of the filing of this petition (without waiver of any claim of the petitioner to tolls, revenues, earnings, income, rents, issues and profits, accruing prior to the filing of this petition) and segregated and sequestered by or under the direction of this Court for the benefit of the petitioner, as trustee, and of the holders of the Bonds and interest obligations secured by said mortgage lien and be applied to and for their benefit, subject only to such expenses and other uses as may legally and properly be incurred in the operation and preservation of said property, having due regard for the rights of the petitioner and the holders of the Bonds and for the protection of the security of said mortgage lien, and that the rights of the petitioner, as trustee, and of the holders of the Bonds and interest obligations may be carefully and fully preserved;

[fol. 415a] 8. That the Railroad Company be required to make answer to all and singular the matters hereinbefore stated and charged, but not under oath, answer under oath being hereby expressly waived, and to stand to and abide by and perform such orders, directions or decrees as shall be made herein and as to this Court shall seem equitable and just; and

9. That the petitioner may have such other and further relief in the premises as the nature and circumstances of

this proceeding may require and as to this Court may seem just and proper.

And the petitioner as in duty bound will ever pray, etc. Dated: November 19th, 1935.

City Bank Farmers Trust Company, as Trustee under the General Mortgage Dated as of February 1, 1924, of The Denver and Rio Grande Western Railroad Company, By Stewart C. Pratt, Vice-President. Ralph Hartzell, First National Bank Building, Denver, Colorado. Mitchell, Taylor, Capron & Marsh, 20 Exchange Place, New York, N. Y., Attorneys and Solicitors for City Bank Farmers Trust Company, as Trustee, etc.

[fol. 415b] *Duly sworn to by Stewart C. Pratt. Jurat omitted in printing.*

Filed Nov. 25, 1935—10:45 A.M. Charles W. Bishop, Clerk.

[fol. 416] In United States District Court

Answer of City Bank Farmers Trust Company, as Trustee, to the Petition of Trustees for Authority to Borrow Money and to Issue Their Certificates of Indebtedness Thereof, Verified June 22, 1936

City Bank Farmers Trust Company, as trustee under the mortgage and deed of trust (hereinafter called the "General Mortgage"), dated as of February 1, 1924, made by The Denver and Rio Grande Western Railroad Company (said Trust Company as such trustee being hereinafter called the "General Mortgage Trustee"), answering the petition herein verified June 22, 1936, of Wilson McCarthy and Henry Swan, as trustees of the property of The [fol. 417] Denver and Rio Grande Western Railroad Company, or so much of said petition as the General Mortgage Trustee is advised is material and is necessary for it to answer, respectfully shows to this Court as follows:

I. The General Mortgage Trustee denies that it has any knowledge or information thereof sufficient to form a belief as to the allegations, or any of them, contained in paragraphs 2 to 9, inclusive, of said petition.

II. The General Mortgage Trustee alleges, upon information and belief, that a number of items included in the "Petition of Trustees for Approval of Certain Expenditures for Improvements" filed herein on March 21, 1936, and in Schedules 1 to 4, inclusive, appended thereto as exhibits, expenditures for which were authorized by an order of this Court entered herein on or about March 21, 1936, and sometimes designated as "Order No. 31", are items that are not essential either (a) for the safe operation of, or (b) for the preservation of, the property subject to the lien of the General Mortgage.

III. The General Mortgage Trustee alleges, upon information and belief, that a number of items included in the "Petition of Trustees for Approval of Additional Expenditures for Improvements" filed herein on April 23, 1936, and in Schedule 5, appended thereto as an exhibit, expenditures for which were authorized by the order of this Court entered herein on or about April 23, 1936, sometimes [fol. 418] designated as "Order No. 44" and entitled "Order Approving and Authorizing Additional Expenditures for Certain Improvements", are items that are not essential either (a) for the safe operation of, or (b) for the preservation of, the property subject to the lien of the General Mortgage.

IV. The General Mortgage Trustee alleges, upon information and belief, that if such items included in said schedules designated as schedules 1 to 5, inclusive, as are not essential either (a) for the safe operation of, or (b) for the preservation of, the property subject to the lien of the General Mortgage, were omitted from the authorizations contained in said Orders Nos. 31 and 44, said trustees would be able to finance all of such expenditures as are essential for said purposes and to make the additional expenditures referred to and described in paragraph 2 of said petition verified June 22, 1936, without the issuance of all or any part of the Trustees' certificates of indebtedness applied for in said petition.

V. The General Mortgage Trustee objects to the issuance of any trustees' certificates of indebtedness, having any lien upon any part of the property covered by the General Mortgage prior to the lien thereon of the General Mortgage, for the purpose of financing any of the expendi-

tures authorized by said Orders Nos. 31 and 44, or for any of the expenditures contemplated by said paragraph 2 of said petition verified June 22, 1936, unless and until there have been eliminated from said Schedules 1 to 5, inclusive, [fol. 419] all items that are not essential for either (a) the safe operation of, or (b) the preservation of, the property subject to the lien of the General Mortgage.

VI. The General Mortgage Trustee denies that this Court has power to authorize the issuance of trustees' certificates of indebtedness, having any lien on any part of the property covered by the General Mortgage prior to the lien thereon of the General Mortgage, for the purpose of financing any of said expenditures unless and until all items included therein that are not essential (a) for the safe operation of, or (b) for the preservation of, the property subject to the lien of the General Mortgage have been eliminated and unless and until it has been established to the satisfaction of this Court that the issuance of such trustees' certificates of indebtedness are essential either (a) for the safe operation of, or (b) for the preservation of, the property subject to the lien of the General Mortgage.

Wherefore, the General Mortgage Trustee respectfully prays:

1. That this Court re-examine the items included in said Schedules 1 to 5, inclusive, for the purpose of eliminating therefrom, and that this Court eliminate therefrom, all items therein included that are not shown to the satisfaction of this Court to be essential either (a) for the safe operation of, or (b) the preservation of, the property subject to the lien of the General Mortgage;

2. That, unless and until such re-examination and such [fol. 420] elimination have been effected, said petition verified June 22, 1936, be in all respects denied; and

3. That the General Mortgage Trustee may have such other and further relief in the premises as the nature of the case may require and as to this Court may seem proper.

City Bank Farmers Trust Company, as trustee under the mortgage and deed of trust dated as of February 1, 1924, made by The Denver and Rio Grande Western Railroad Company, by Ralph E.

Morton, Trust Officer; Mitchell, Taylor, Capron & Marsh, 20 Exchange Place, New York, N. Y.; Ralph Hartzell, First National Bank Building, Denver, Colorado; Solicitors for City Bank Farmers Trust Company, as trustee as aforesaid.

[fol. 421] *Duly sworn to by Ralph E. Morton. Jurat omitted in printing.*

Filed July 17, 1936, 10:35 A.M. Charles W. Bishop, Clerk.

[fol. 422] The Denver and Rio Grande Western Railroad Company

The Denver and Salt Lake Western Railroad Company
The Denver and Salt Lake Railway Company
The Rio Grande Junction Railway Company
Goshen Valley Railroad Company

PROPOSED PLAN OF CONSOLIDATION AND REORGANIZATION AS OF JANUARY 1, 1937

Interstate Commerce Commission
Finance Docket No. 11002

Pierce & Greer, 35 Wall Street, New York, N. Y.
Hodges, Wilson & Vidal, Equitable Bldg., Denver Colorado, of Counsel.
July 28, 1936.

[fol. 423] The Denver and Rio Grande Western Railroad Company
The Denver and Salt Lake Western Railroad Company
The Denver and Salt Lake Railway Company
The Rio Grande Junction Railway Company
Goshen Valley Railroad Company

Proposed Plan of Consolidation and Reorganization as of January 1, 1937

I

Historical Introduction

The Denver and Rio Grande Western Railroad Company is the successor to two principal previous companies,

The Denver and Rio Grande Railroad Company and The Rio Grande Western Railway Company.

The first of these two predecessor companies was incorporated in 1870 to acquire and construct a line of railroad in Colorado and New Mexico. It was reorganized in 1886 and its properties conveyed to The Denver and Rio Grande Railroad Company, which executed its Consolidated Mortgage (the bonds issued thereunder hereinafter referred to as the D&RG Consols) as a part of the reorganization plan in that year.

The second of the predecessor companies above mentioned originated in The Denver and Rio Grande Western Railway Company, which was incorporated in 1881 to acquire and construct a line of railroad from Ogden, Utah, to the Utah-Colorado State line, with branches. That company was reorganized in 1889 and its properties transfer-
[fol. 424] red to The Rio Grande Western Railway Company, which executed its First Trust Mortgage (the bonds issued thereunder hereinafter referred to as the RGW First Trust 4s) as a part of the reorganization plan in that year. Ten years later it executed its First Consolidated Mortgage (the bonds issued thereunder hereinafter referred to as the RGW Consols).

Very close relations obtained between these two predecessor companies, and in 1904, because of the practical closing of the Ogden gateway to through traffic to and from California, they entered into an investigation of the feasibility of an independent line from Salt Lake City to San Francisco. As a result of this investigation, the managements decided to assist in promoting the plans of The Western Pacific Railway Company, and agreed to guarantee an issue of $50,000,000 First Mortgage Bonds of the latter company, while the RGW agreed to purchase sufficient second mortgage bonds of that company to ensure the completion of the line. In connection with this agreement, the D&RG and the RGW were to receive 2/3 of the capital stock. A traffic agreement was also entered into providing for a joint through line from Denver to San Francisco. In 1908 the D&RG and RGW were formally consolidated into a new corporation known as The Denver and Rio Grande Railroad Company. This company succeeded to the obligations of both predecessor companies with respect to the Western Pacific Railway Company. A receivership and reorganization of the Western Pacific in

1915 led directly to the loss of the Western Pacific and to [fol. 425] a reorganization of The Denver and Rio Grande Railroad Company of 1908. This reorganization was effectuated by conveying its properties in 1920 to a new corporation organized at that time in Delaware for the purpose, The Denver and Rio Grande Western Railroad Company, (hereinafter referred to as the D&RGW) which is the present company.

The reorganization of 1920 did not reduce the fixed charges of the company, and a further reorganization became necessary in 1922 and was effectuated in 1924. As a part of this reorganization the company executed its Refunding and Improvement Mortgage (to provide for new money and future financing) and its General Mortgage (to provide for the old bonds which were readjusted by the plan).

II

Location of Properties

The main line of the company extends from Ogden and Salt Lake City on the west (where it connects with the Western Pacific, the Union Pacific and the Southern Pacific) to Pueblo and Denver on the east (where it connects with the Missouri Pacific, the Burlington, the Rock Island, the Union Pacific, the Santa Fe and the Colorado and Southern). In addition there are a large number of branch lines, particularly in Colorado. The branch lines in Colorado include a substantial mileage of narrow gauge line. These matters are more fully shown on a map, attached hereto marked Exhibit A.

[fol. 426] For the purpose of mortgage liens the system may be roughly divided into two halves at Crevasse, Colorado, a point near the Utah-Colorado State line. The properties west of Crevasse represent, generally speaking, the properties acquired from the RGW of 1889 and are subject to the RGW First Trust 4s as a first lien and the RGW Consols as a second lien. The RGW Consols are also a first lien on the entire capital stock of the Utah Fuel Company. The properties east of Crevasse represent, generally speaking, the properties acquired from the D&RG of 1886 and are subject to the D&RG Consols as a first lien. The Refunding and Improvement Mortgage is a lien junior to all of the above, and the General Mortgage is a lien junior

thereto. Certain branch lines on both halves of the system are subject to different mortgages as a first lien, depending on the date of construction or acquisition.

An essential link in the main line of the eastern half (about 62 miles, between Grand Junction and Rifle, Colorado) is owned by the Rio Grande Junction Railway Company. $2,000,000 principal amount of its First Mortgage Bonds (hereinafter referred to as the RGJ 5s) are outstanding in the hands of the public. All of a junior issue of bonds and all of the stock are pledged under the Refunding and Improvement Mortgage. The properties are operated by the D&RGW under lease.

A small amount of equipment trust certificates is outstanding, and the lien on the equity in such equipment is held by the Refunding and Improvement Bonds. The lien [fol. 427] on most of the remaining equipment is held by the D&RG Consols and the Refunding and Improvements.

In the reorganization of 1924 it was realized that the proper growth of the properties would require the development of a short line between Dotsero and Denver, Colorado, and a policy to favor such a development was written into the reorganization plan and the by-laws of the reorganized company.

III.

The Dotsero Cutoff

The Denver and Salt Lake Railroad Company owned a line of railroad extending from Utah Junction (near Denver) in a westerly direction to Craig, Colorado. As a result of difficult operating conditions over the continental divide and lack of traffic, the road went into receivership in 1917.

There had been public agitation for many years in Denver to construct a tunnel under the continental divide with public funds. Spurred by the probability that otherwise the Denver and Salt Lake Railroad might be abandoned, this movement finally came to a head in 1922, and the tunnel was constructed by the Moffat Tunnel Commission. This tunnel made possible satisfactory operating conditions across the continental divide, and opened up the possibility of developing the Denver and Salt Lake into a transcontinental route.

As a result that company was reorganized in 1926, and its properties transferred to the present company, The Denver and Salt Lake Railway Company (hereinafter [fol. 428] referred to as the D&SL). The Moffat Tunnel was leased to the D&SL in the same year. Soon afterwards the D&SL organized a subsidiary, The Denver and Salt Lake Western Railroad Company (hereinafter referred to as the D&SLW) to construct a line of railroad from Bond-Orestod to Dotsero, Colorado, in order to connect with the line of the D&RGW and promote full utilization of the Moffat Tunnel.

Carrying out the policy expressed in its reorganization plan, the D&RGW asked and obtained authority from the Interstate Commerce Commission (1) to acquire all of the stock of the D&SLW and to take a lease of its line, and (2) to acquire all of the stock of the D&SL and to enter into a trackage agreement permitting joint operation over its line between Orestod and Utah Junction. Authorization was conditioned on purchasing all shares of the D&SL and on completing construction of the D&SLW line within a designated time. Accordingly, 29,470 shares of D&SL stock were purchased.

In order to complete the project outlined by the Commission, the D&RGW borrowed from Reconstruction Finance Corporation (hereinafter referred to as RFC) $3,631,000 to finance the purchase of the D&SLW stock and the construction of its line, and $3,110,850 to finance the purchase of the remaining shares of D&SL stock, both loans to bear interest at the rate of 5% per annum (later reduced to 4%). All shares of stock so purchased, and the D&SL shares previously purchased by it with its own funds, were pledged as security for these obligations.

[fol. 429] Subject to such pledge, the D&RGW thus owned all the stock of D&SLW (and operated its properties under lease) and virtually all the stock of the D&SL (and operated over a part of its line under a trackage agreement). The D&SLW line was completed and operation over the Dotsero Cutoff was begun on June 15, 1934.

IV

Present Capitalization

The D&RGW now has the following securities outstanding (excluding pledged bonds and short term debt):

	Principal	Annual Interest
Equipment Trusts	$1,805,000	$68,408
RGW First Trusts (4%)	15,190,000	607,600
RGW Consols (4%)	15,080,000	603,200
D&RG Consols (4%)	34,125,000	1,365,000
D&RG Consols (4½%)	6,382,000	287,190
D&RGW Refunding and Improvements (6%)	2,000,000	120,000
D&RGW Refunding and Improvements (5%)	12,000,000	600,000
D&RGW Generals (5%)	29,808,000	1,490,400
Preferred Stock	16,445,600	
Common Stock (300,000 shares of no par value)	62,457,540	
		$5,141,798

[fol. 430] In addition there are outstanding $2,000,000 principal amount of RGJ 5s, on which the annual interest is $100,000, thus bringing fixed interest requirements to $5,241,798 per year.

Beginning in 1932 the D&RGW was compelled to borrow short term funds in order to continue service on the above obligations. For those and general corporate purposes it borrowed (1) $1,500,000 from the Chase National Bank, all of which is now unpaid and outstanding, bearing interest at 5%; (2) $500,000 from The Railroad Credit Corporation, $340,923 of which was outstanding as of May 31, 1936, bearing interest at 1½%; and (3) $3,950,000 from the RFC, all of which is now unpaid and outstanding, bearing interest at 6% (later reduced to 4%). The two other loans from RFC ($3,631,000 for construction of the D&SL-W and $3,110,850 for acquisition of D&SL) have already been mentioned. The total of these loans is $12,532,773 and annual interest thereon at the above rates is $507,788, thus bringing the total fixed interest requirements to $5,749,586.

The Company's total current liabilities as of May 31, 1936, consisted of the following:

[fol. 431]

Account	
758—Loans and bills payable	$ 6,936,773
759—Traffic and Car Service balances payable	668,656
	668,656
760—Audited accounts and wages payable	8,746,073
761—Miscellaneous accounts payable	24,187
762—Interest matured unpaid	9,055,273
764—Funded debt matured unpaid	43,385,100
766—Unmatured interest accrued	1,761,275
767—Unmatured rents accrued	315,447
768—Other current liabilities	21,238
	$70,914,024

The RGJ has issued no securities other than the $2,000,000 principal amount of RGJ 5s outstanding and the bonds and stock pledged under the Refunding and Improvement Mortgage. The D&SLW has no securities outstanding other than the common stock above mentioned. The D&SL has outstanding in addition to the common stock above mentioned, $1,500,000 principal amount of First Mortgage 4s (redeemable at 101) and $11,000,000 principal amount of Income Mortgage 6s (redeemable at 102), which would become a fixed charge in the event of a merger or consolidation with the D&RGW. There are likewise outstanding $2,217,000 principal amount of The Northwestern Terminal Railroad Company First Mortgage Income 5s (redeemable at 102); the properties of that com-
[fol. 432] pany are operated by the D&SL under lease, and interest on its bonds would become a fixed charge in the event of a merger or consolidation of the D&SL with the D&RGW. Present rental paid by the D&SL for its use of the property of The Northwestern Terminal Railroad Company is based on 2% per annum on the First Mortgage Income Bonds, which amount is subject to increase with increases in the traffic of the D&SL.

V

Earnings

The operating revenues and the net income available for interest of the D&RGW since the reorganization of 1924 are as follows:

Year	Operating Revenues	Net Income Available for Interest
1924	$33,011,557	$2,785,660
1925	33,629,463	6,799,142
1926	34,030,308	7,711,952
1927	33,121,168	6,475,860
1928	33,200,656	7,317,286
1929	34,828,668	8,839,182
1930	29,747,537	7,119,659
1931	23,484,818	5,204,504
1932	17,560,621	2,894,579
1933	17,112,793	3,398,795
1934	19,246,850	2,600,278
1935	20,944,229	2,459,364

On a consolidated basis including the Rio Grande Junction, the net income available for interest would be increased $100,000 per annum.

[fol. 433] Operating revenues for the first five months of 1936 were $9,171,663 compared with $7,320,764 for the same period in 1935. Corresponding figures for net income available for interest were $197,195 and $405,619 respectively.

The operating revenues and the income available for interest of the D&SL since the opening for operation of the Moffat Tunnel in February, 1928, are as follows:

Year	Operating Revenues	Net Income Available for Interest
1928	$4,011,663	$1,202,707
1929	3,981,131	1,420,104
1930	3,197,282	841,328
1931	2,302,835	835,976
1932	1,915,469	566,453
1933	1,657,331	432,506
1934	1,620,006	602,591
1935	2,234,882	899,950

Operating revenues for the first five months of 1936 were $1,100,123, compared with $670,678 for the same period in 1935. Corresponding figures for net income available for interest were $216,526 and $249,422 respectively.

VI

Reorganization Proceedings

As a result of the abrupt decline in earnings and in net income available for interest which began in 1932, the D&RGW was forced to borrow short term funds as above [fol. 434] stated, and upon the exhaustion of its credit, it filed a petition for reorganization under Section 77 of the Bankruptcy Act. Such petition was filed on November 1, 1935, in the District Court of the United States for the District of Colorado, and Trustees appointed by that Court have subsequently administered the property. A similar petition was filed at the same time in the same Court by the D&SLW, and a separate Trustee was appointed by that Court.

When the necessity for a reorganization became apparent, the D&RGW undertook exhaustive studies into the earnings of the properties by mortgage divisions and other factors underlying a reorganization. It has continued those studies since the filing of the petitions in bankruptcy. It has held numerous conferences with the holders of large amounts of the respective issues of its bonds and other creditors in order to develop a plan. The object has been to provide a new capital structure for the properties, safely within their ability to support, and apportioned among the existing security holders and other creditors on the basis of the respective seniorities of their position. These studies and conferences have materially aided in the development of this plan of reorganization.

This plan of reorganization is being filed by the Company before the District Court of the United States for the District of Colorado and the Interstate Commerce Commission, under and pursuant to subdivision (d) of Section 77 of the Bankruptcy Act, as amended.

[fol. 435] VII

General Characteristics of Plan

The plan provides for a consolidation of the physical properties of the D&RGW, the D&SLW, the D&SL, the RGJ and the Goshen Valley Railroad Company, (the latter a small branch line in Utah), so that the new company will own in fee continuous transcontinental routes from Denver and Pueblo on the east to Salt Lake City and Ogden on the west via the Moffat Tunnel and the Royal Gorge.

Due to the changes in operating conditions and earning power of this property resulting from the construction of the Moffat Tunnel and the Cutoff, no extensive period of time is available which is representative of the earnings of this consolidated property under these latest conditions. However, a close analysis of the conditions during the years 1932, 1933 and 1934 justifies the belief that the average net income of the consolidated property during those three low years of the depression would have been slightly in excess of $3,000,000 per annum if the Cutoff and tunnel had both been in operation during that period. The actual net income which would have been available for interest on the consolidated property during the calendar year 1935 was $3,479,521. In the interests of a conservative plan and to guard against the possibility of any subsequent temporary reduction in earnings it is proposed that the total fixed interest charge of the new company be $2,358,445, which amount would have been covered 1.47 times in 1935.

The plan also provides for an issue of Income Bonds so [fol. 436] limited in amount that it is believed that the bonds presently to be issued would have had their interest earned and paid during the calendar year 1935 if the consolidated property had been operating as a unit in that year.

The underlying bonds which cannot be offered fixed interest bearing securities or income bonds (being portions of the D&RG Consols and Refunding and Improvements) are offered first preferred stock. The General Mortgage Bonds and the present Preferred Stock are offered a participating preferred stock in varying proportions. Present common stockholders will agree to cancellation of certain bonds now held by them, will agree to subscribe to new fixed interest bearing bonds in order to provide new capital, and will receive the new common stock,

The allocation of the various issues of bonds to the present bondholders has been based on an exhaustive study of the earnings of the property segregated by mortgage districts during the 12 months ended June 30, 1935, being the first 12 months subsequent to the opening of the Cutoff. In allocating revenues as between mortgage districts a mileage prorate has in all instances been used, except that the Cutoff and the operations under trackage rights by the D&RGW over the line of the D&SL have been allocated revenues on the basis of mileage over the old line from Dotsero to Denver through Pueblo in recognition of——

(1) difficult operating conditions over the D&SL.

(2) abnormally high costs of maintenance on the [fol. 437] D&SL during 1934 and 1935, because of unusual improvement work which will probably continue for several years.

(3) high rental necessary to be paid to the Moffat Tunnel Commission for the use of the Moffat Tunnel.

(4) undeveloped condition of the traffic via this route in 1934 and 1935 as compared with the prospective future development of such traffic.

Original estimates made in 1928 before the construction of the Cutoff was undertaken indicated that it would take five years to develop the normal amount of traffic via this route. Despite the generally lower level of business in 1934 and 1935 as compared with 1928, the volume of traffic over the Cutoff during its first year in operation was fully up to the expectations of 1928.

Even on this basis the earnings from the D&SL and the operations of the D&RGW between Denver and Dotsero by the new route are not sufficient entirely to support the interest charges on the refunded obligations of the D&SL as hereinafter set forth and on the new First and Refunding Bonds offered to the RFC, if the same earnings ratios are applied to these properties as were applied to the other mortgage districts. To the extent that these proposed fixed charges are not presently covered by the earnings of the underlying properties and the other collateral, they have been allocated for support to the RGW First Trust 4s of 1939 and to the RGJ 5s of 1939, these being the only two [fol. 438] mortgage districts which have benefited from the

Cutoff and which will benefit to a greater extent as the business over the Cutoff increases.

In the set-up of allowances for rental of equipment as between the different mortgage divisions, the Refunding and Improvement Bonds have been considered to hold a first lien on equipment acquired since the consolidation of 1908 with the proceeds of

> Refunding and Improvement Bonds;
> Equipment Trust certificates;
> Purchase money agreements; and
> Other bonds later refunded by the Refunding and Improvement Bonds, or by bonds junior thereto;

together with all other equipment acquired subsequent to the date of the Refunding and Improvement Mortgage. The remaining equipment acquired since the consolidation of 1908 has been considered to be subject to a direct first lien of the D&RG Consols.

In estimating the income available to the consolidated company for interest on the Income 4s, consideration has been given to the probable savings in overhead expenses which will result from the consolidation, to the reduced net income resulting from the sale of government securities by the D&SL in connection with its refunding operations during the latter part of 1935, and to the increased rental which it will be necessary to pay for the use of the property of the Northwestern Terminal as a result of the consolidation. The consolidated company will have six months after the [fol. 439] effective date of consolidation to decide whether it wishes to continue to lease the property of the Northwestern Terminal at the increased rental, but in order to be conservative present calculations are based on the payment of the full increase.

At the suggestion of the Chairman of the Board of the Reconstruction Finance Corporation, considerable study has also been given to the inclusion of the properties of the Western Pacific Railroad Company in the new consolidated company, but this is not proposed at this time. A special committee of the Board of Directors of the D&RGW has been appointed, with authority to negotiate such a consolidation, and this plan has been so drafted that if a consolidation with the Western Pacific can subsequently be worked out so as finally to achieve the purposes in mind

in 1904 when the construction of that company was originally undertaken, such consolidation can be made effective without resetting the capital structure of the new company. In that event a supplemental plan modifying the plan now presented will be filed.

The provisions of the plan in detail are set out below:

[fol. 440] VIII

Proposed Capitalization of New Company

Fixed Interest bearing debt:	
Equipment trust obligations remaining undisturbed	$ 1,805,000
Western Division First Mortgage 3½% Bonds	22,680,233
First and Refunding Mortgage 4% Bonds (incl. $792,000 pledged)	37,405,730
Total fixed interest bearing debt	$61,890,963
Contingent Interest bearing debt: (excl. $1,558,000 Ten Year Collateral Notes)	
General Income Mortgage 4% Bonds (incl. $766,000 of $2,479,000 pledged)	$22,063,886
Total debt	$83,954,849
First Preferred Stock, $100 par value, 4½% dividends (excl. $2,825,000 pledged)	$33,208,618
Participating Preferred Stock, $1 par value, $5 dividends (No. Shares) at least	413,842
Common Stock, $1 par value (No. Shares)	200,000
Western Division First Mortgage 3½% Bonds —Series A	$22,680,233

The Western Division First Mortgage will be a direct first lien on all the existing railroads, equipment and track-[fol. 441] age rights now subject to the lien of the Rio Grande Junction First Mortgage and the Rio Grande Western First Trust Mortgage, together with a direct first lien on that portion of the main line of the D&RGW now subject to the lien of the D&RG Consolidated Mortgage lying between Dotsero and Rifle, and between Grand Junction and Crevasse, all in the state of Colorado.

Bonds may be issued under this mortgage up to, but not in excess of $40,000,000. The balance not presently issued under the plan may be issued for not to exceed 75% of the

cost of additions and betterments to the mortgaged property, or in exchange for First Mortgage Bonds of The Western Pacific Railroad Company in connection with the extension of the lien of the mortgage over the entire line of that company in the event of a possible future consolidation. Such additional bonds may be of various series, all equally secured as to principal and interest, but may have different interest rates, maturities and other provisions.

The Series A Bonds presently to be issued will mature in 40 years from date of issue, and bear interest which will be a fixed charge at the rate of 3½% per annum. They will be redeemable in whole or in part upon 30 days notice at any interest date, and at 60 days notice at any other date, at par plus accrued interest.

[fol. 442] *First and Refunding Mortgage Bonds, Series A (Including Pledged Bonds)* $37,405,730

It is proposed that the company also execute a First and Refunding Mortgage, which will be a direct lien on all the existing standard gauge railroads, equipment and trackage rights of the companies proposed to be consolidated, subject only to the lien of the Western Division First Mortgage.

The mortgage will be open-end for future financing, and will permit the issuance of various series of bonds, all equally secured as to principal and interest, which may have different interest rates, maturities and other provisions. Additional First and Refunding Bonds may be issued to finance not to exceed 75% (except as otherwise provided in the plan) of the cost of additions and betterments to the company's property not otherwise financed, to refund the $2,217,000 First Mortgage 5% Income Bonds of The Northwestern Terminal Railroad Company, and in exchange for outstanding securities of The Western Pacific Railroad Company in the event of a consolidation with that company. First and Refunding Bonds not to exceed $40,000,000 will be reserved to refund the Western Division First Mortgage Bonds which may be issued.

The Series A First and Refunding Bonds presently to be issued will mature in 60 years from date of issue, and bear interest which will be a fixed charge at the rate of 4% per annum. They will be redeemable in whole or in part upon [fol. 443] 30 days' notice at any interest date, and on 60

days' notice at any other date, at the following prices, plus accrued interest:

105 for the first 10 years;
104 " " next 10 "
103 " " " 10 "
102 " " " 10 "
101 " " " 10 " ; and
100 thereafter.

They will be callable at par and accrued interest for the retirement fund at any time.

The bonds presently to be issued will provide, effective immediately, for a non-cumulative debt retirement fund of ½% of the maximum principal amount of First and Refunding Bonds at any previous time outstanding, plus interest on the bonds already purchased, which shall be kept alive in the fund, all to become payable annually if earned after payment of interest on the First and Refunding Bonds still outstanding. This fund shall be devoted exclusively to the retirement of Series A Bonds held by the RFC so long as any such bonds are held by that Corporation. In addition, all distributions from the Marshalling and Distributing Fund of the RCC shall be paid into the retirement fund.

Subsequent to the retirement of all First and Refunding Bonds held by the RFC, the fund shall be devoted to the purchase in the open market of the bonds at the lowest price obtainable. If no First and Refunding Bonds can be so purchased at par or less than par, the retirement fund may [fol. 444] at the option of the company be devoted to the retirement of First and Refunding Bonds through call at par, or to the retirement through purchase in the open market of General Income Mortgage Bonds. Accrued interest at time of purchase on bonds acquired for the fund shall be paid from income of the company and not from the retirement fund.

$6,000,000 First and Refunding Bonds shall be placed in the treasury of the new company upon reorganization to provide funds for 100% of the cost of additions and betterments to the property and other proper corporate purposes during the first year after reorganization, $3,000,000 of which shall be available for immediate sale, the remaining

$3,000,000 to be available for sale to the Missouri Pacific and Western Pacific as required.

Before computing the amount of income available for retirement funds on First and Refunding Bonds and charges junior thereto, there shall be set aside out of the income of the company remaining after payment of interest on the First and Refunding Bonds and senior obligations, the sum of $350,000 per annum, which may be used during the ensuing 12 months for additions and betterments to the property of the company. Any portion of this $350,000 remaining unexpended at the end of the year may be accumulated for use in future years at the discretion of the Board.

General Income Mortgage Bonds—
Series A—(Including $766,000 *of pledged bonds)* $22,063,886

[fol. 445] It is proposed that the new company also execute a General Income Mortgage (hereinafter called "General Mortgage" for convenience) which will be a lien upon all of the property upon which the First and Refunding Mortgage is a lien, subject to the liens of the Western Division Mortgage and the first and Refunding Mortgage. It shall also be a first lien upon the capital stock of the Utah Fuel Company, subject to existing rights of redemption of such stock.

The General Mortgage will be open-end for future financing, and will permit the issuance of various series of bonds, which may or may not be equally secured as to principal and interest, which may have different interest rates, maturities, conversion rights and other provisions, except that no additional series may be created prior in lien to Series A.

The Series A Bonds presently to be issued will mature 75 years from date of issue, and bear interest at the rate of 4% per annum. They will be redeemable in whole or in part at par and payable interest accrued. Any income of the company remaining after payment of interest and retirement fund on prior obligations will be used for the payment of interest on the Series A Bonds. Interest shall be paid only in multiples of ½%, fractions of ½% remaining to be paid into the general funds of the company. Interest on the Series A Bonds will be cumulative for not to exceed two years' interest.

The mortgage will provide for a debt retirement fund of ¼% of the maximum principal amount of Series A Bonds

[fol. 446] at any previous time outstanding, similar in other respects to the debt retirement fund provided for the First and Refunding Bonds. Payments into the debt retirement fund are to be made only after payment of all interest due has been made on the Series A Bonds.

In computing the income of the company available for debt retirement on the Series A Bonds there shall be deducted after payment of interest on such bonds, an annual amount representing the difference between 3% of the railway operating revenues of the new company and $350,000, which sum shall be set aside from the income of the company for additions and betterments to the company's property during the ensuing 12 months. Any balance of this fund remaining unexpended during such 12 months' period may be accumulated in the manner already described with respect to the additions and betterments fund of $350,000 per annum previously mentioned.

Both of the additions and betterments funds described may be used to defray any portion of the cost of additions and betterments to the company's property.

Registered holders of Series A Bonds shall have one vote per $1000 bond in voting for the election of two of the company's directors.

Ten-Year Collateral Notes— $1,558,000

It is proposed that the new company issue a series of one or more notes, secured by certain collateral as hereinafter set forth, maturing on or before ten years from date of [fol. 447] issue, but renewable from time to time at the option of the company for ten year periods until retired as set forth in the agreement securing the notes. The notes will be entitled only to such income as is paid by the company upon the collateral securing such notes. The notes will be cumulative to the extent of two years interest thereon, which will be at the rate of 4% per annum. Any income paid upon collateral which is in excess of the interest requirements on the notes after payment of all accumulations shall be applied to reduction of the principal amount of such notes at par and accrued interest. The notes will be callable in whole or in part at any time on thirty days' notice at par and accrued interest. Upon the retirement or call of the last of such notes the collateral securing them shall be returned to the treasury of the company.

THE DENVER AND SALT LAKE RAILWAY COMPANY
THE RIO GRANDE JUNCTION RAILWAY COMPANY
GOSHEN VALLEY RAILROAD COMPANY

Exhibit B

PROPOSED PLAN OF CONSOLIDATION AND REORGANIZATION AS OF JANUARY 1, 1937

EXISTING CAPITALIZATION	Amount	Undisturbed	Western Division First Mortgage Bonds Series A—3½% Maturity: 40 Years	First and Refunding Mortgage Bonds Series A—4% Maturity: 60 Years	General Income Mortgage Bonds Series A—4% Maturity: 75 Years	First Preferred Stock 4½% Par Value $100 per Share	Participating Preferred Stock Par Value $1 $5 Dividend (No. Shares
The Denver and Rio Grande Western Railroad Company:							
Equipment Trust Certificates	$ 1,805,000	$ 1,805,000	$	$	$	$	
R. G. J. 5s, 1939, Principal	2,000,000		(Note A) 2,000,000				
Unpaid Interest	158,333		(7.92%) 158,333				
R. G. W. Trust 4s, 1939, Principal	15,190,000		(Note B) 15,190,000				
Unpaid Interest	1,215,200		(8.00%) 1,215,200				
D. & R. G. Consol. 4s, 1936, Principal	34,125,000		(10%) 3,412,500	(15%) 5,118,750	(15%) 5,118,750	(60%) 20,475,000	
Unpaid Interest	3,412,500					(6.66%) 2,274,140	
D. & R. G. Consol. 4½s, 1936, Principal	6,382,000		(10%) 638,200	(15%) 957,300	(15%) 957,300	(60%) 3,829,200	
Unpaid Interest	717,975					(7.50%) 478,469	
R. G. W. Consol. 4s, 1949, Principal	15,080,000			(40%) 6,032,000	(60%) 9,048,000		
Unpaid Interest	1,357,200				(8.25%) 1,244,836		
D. & R. G. W. Ref. and Impr. 5s, 1978, Principal	12,000,000			(15%) 1,800,000	(40%) 4,800,000	(45%) 5,400,000	
Unpaid Interest	1,350,000					(6.27%) 751,809	
Reconstruction Finance Corp. Debt, 4%, Principal	10,691,850			10,691,850			
Unpaid Interest	626,108			391,150			
The Railroad Credit Corp. Debt, 1½% (Est.)	328,000		66,000	(Note C) 179,000	83,000		
Bank Debt, 5%, Principal (Note D)	1,500,000			792,000	708,000		
Unpaid Interest	93,948				58,000		
D. & R. G. W. General 5s, 1955, Principal	29,808,000						29
Unpaid Interest	12,544,200						3
Preferred Stock	16,445,600					(50%)	8
D. & R. G. W. Ref. and Impr. 6s, 1974, Principal	2,000,000						
Unpaid Interest	270,000						
Common Stock	Shs 300,000						
Total Capitalization		1,805,000	22,680,233	25,962,050	22,017,886	33,208,618	41
Charges		68,408	793,808	1,038,482	860,715	1,494,388	$ 2,0
Charges—Cumulative		68,408	862,216	1,900,698	2,781,413	4,275,801	$ 6,3
The Denver and Salt Lake Railway Company:							
First 4s, 1960, Principal	1,500,000			(101%) 1,515,000			
Income 6s, 1960 (with public), Principal	9,734,000			(102%) 9,928,680			
Stock (with public)	Shs 460				46,000		
Total Capitalization				11,443,680	46,000		
Charges				457,747	1,840		
Charges—Cumulative				457,747	459,587	459,587	$ 459
The Denver and Rio Grande Western Railroad Company—The Denver and Salt Lake Railway Company							
Grand Total Capitalization		1,805,000	22,680,233	37,405,730	22,063,886	33,208,618	41
Charges		68,408	793,808	1,496,229	882,555	1,494,388	$ 2,0
Charges—Cumulative		68,408	862,216	2,358,445	3,241,000	4,735,388	$ 6,8

Note A—Also offered 4.375% or $87,500 in cash to compensate for loss of interest to maturity.

Note B.—Also offered 1.25% or $189,875 in cash to compensate for loss of interest to maturity.

Note D.—Is offered a 10-year income note in the face amount of $1,558,000 secured by $792,000 principal amount of First and Refunding Bonds, by $766,000 principal amount of Income 4s, and by other collateral, all as set forth in the plan.

Not

July 28, 1936.

Filed July 29, 1936 - 12 noon - Charles W. Bishop, Clerk

First Preferred Stock (excl. pledged stock) $33,208,618

It is also proposed that the new company issue First Preferred Stock which will permit additional issues for future financing, and will be issuable in various series which may have different dividend rates, conversion rights, and other provisions. The First Preferred Stock presently to be issued will have a par value of $100 per share, and will be entitled to annual non-cumulative dividends of 4½%.

It will be redeemable in whole or in part at par plus payable dividends declared.

Holders of First Preferred Stock shall have one vote [fol. 448] per share in voting for the election of two of the company's directors.

Participating Preferred Stock— 413,842 *shares*

It is also proposed that the new company issue Participating Preferred Stock which will permit additional issues for future financing and will be issuable in various series, which may have different dividend rates and other provisions. The Participating Preferred Stock presently to be issued will have a par value of $1 per share and will be entitled to annual non-cumulative dividends of $5 per share, and will also participate equally with the common stock after dividends of $4 per share on the latter. It will be redeemable in whole or in part at $100 per share, plus payable dividends declared, and will be entitled to $100 in liquidation.

The additions and betterments funds heretofore described will operate prior to the appropriation of the income of the company for preferred stock dividends regardless of whether there are any General Mortgage Bonds outstanding or not.

Holders of preferred stock shall have one vote per share in voting for the election of two of the company's directors.

Common Stock— 200,000 *shares*

The new common stock will have a par value of $1 per share, and will be entitled to elect 9 of the company's directors, one of whom shall be the president.

[fol. 449] Board of Directors

The Board of Directors of the Company shall consist of 15 members. As outlined above, two of these shall be

elected by the registered holders of General Income Mortgage Bonds, Series A; two by the holders of First Preferred Stock; two by the holders of Participating Preferred Stock; and nine by the holders of common stock. One of the directors elected by the common stock shall be the president of the new company.

IX

Treatment of Existing Securities and Obligations

The proposed treatment of existing securities and obligations is outlined on the attached sheet, marked Exhibit B.

Equipment Trusts—		$1,805,000
Equipment trusts are left undisturbed.		
RGJ First 5s, 1939—		$2,000,000
RGW First Trust 4s, 1939—		
Outstanding	$15,190,000	
Pledged RFC	10,000	$15,200,000

New Western Division 3½s are allocated for all of these bonds, together with all of the unpaid interest on such obligations. In addition, holders of these bonds are offered cash to compensate for the difference between 3½% per annum and the present interest rate on these bonds to maturity.

The interest on bonds of these issues was earned approximately three times over during the 12 months ended [fol. 450] June 30, 1935, and it is believed that the creation of this Western Division Mortgage, whose principal lien is on the line securing these two bond issues, will continue to give these bondholders a security as good from an earnings standpoint as that which they now hold, and at the same time meet the problems incident to the early maturity of these bonds presently outstanding.

D&RG Consol 4s *and* 4½s, 1936—			
Outstanding—4s	$34,125,000		
4½s	6,382,000		$40,507,000
Pledged—4s—RFC	783,000		
RCC	662,000		1,445,000
			$41,952,000

These bonds are a lien, among other things, on the main line between Dotsero and Rifle, Colorado, and Grand Junction and Crevasse, Colorado, totalling about 63 miles, which goes to make up part of the continuous main line subject to the lien of the Western Division Mortgage. Western Division Mortgage Bonds issued to the RGW Trust 4s are at the rate of approximately $60,000 per mile of main line. Applying this same rate to the mileage contributed by the D&RG Consols permits the issuance of approximately 10% of the principal amount of the latter bonds in the new Western Division 3½% Bonds.

In allocating First and Refunding Bonds to these bondholders and to other issues it has been assumed that the [fol. 451] fixed charges should have been covered approximately 1.45 times in 1935, which would have been approximately 1.25 times during the three years 1932-1934, inclusive. The earnings available for interest on the D&RG Consols in 1935 were $663,690 (all such earnings figures were actually calculated on the basis of the year ended June 30, 1935, and were substantially the same as for the calendar year 1935). This figure includes an adjustment to compensate for an abnormally low potato crop in the San Luis Valley in the year ended June 30, 1935. This crop was much more nearly normal during the calendar year, and is ordinarily a traffic not subject to violent fluctuations. The figure also includes an adjustment for backshop and heavy repair facilities subject to the lien of this mortgage and used to repair equipment used on other mortgage divisions.

Applying the desired earnings coverage in 1935 will permit the issuance of 15% of First and Refunding 4s to this issue.

In allocating income bonds to the D&RG Consols and to other issues it has seemed desirable to limit the amount of income bonds outstanding to a total on which the full interest could have been paid during the calendar year 1935 if the companies had been consolidated under corporate management. On this basis 10% of Income Bonds could be allocated to the holders of D&RG Consols. This amount is affected by the controversy which exists as to the respective liens on a portion of the company's equipment. The position taken by the Debtor is as heretofore outlined. If [fol. 452] the position which the Debtor understands to be that of the D&RG Consols should be recognized, these bonds

ag rs	General Income Mortgage Bonds Series A—4% Maturity: 75 Years		First Preferred Stock 4½% Par Value $100 per Share		Participating Preferred Stock Par Value $1— $5 Dividends (No. Shares)		Common Stock Par Value $1 per Share (No. Shares)
	$		$				
18,750	(15%)	5,118,750	(60%)	20,475,000			
			(6.66%)	2,274,140			
57,300	(15%)	957,300	(60%)	3,829,200			
			(7.30%)	478,469			
12,000	(60%)	9,018,000					
	(8.25%)	1,244,836					
00,000	(40%)	4,800,000	(45%)	5,400,000			
			(6.27%)	751,809			
01,850							
01,150							
9,000		83,000					
12,000		708,000					
		58,000					
						298,060	
						33,534	
					(50%)	82,228	
							200,000
0,050		22,017,886		33,208,618		413,842	200,000
5,482		880,715		1,494,388	$	2,069,210	
0,698		2,781,413		4,275,501	$	6,345,011	
5,000							
8,680							
		46,000					
3,680		46,000					
7,747		1,840					
7,747		459,587		459,587	$	459,587	
1,730		22,063,886		33,208,618		413,842	200,000
6,229		882,555		1,494,388	$	2,069,210	
8,445		3,241,000		4,735,388	$	6,801,598	

rest to maturity.

cured by $792,000 principal amount of First and other collateral, all as set forth in the plan.

Note C.—Includes $73,000 for 60% of Distributive Share.

Clerk

7-30

would be entitled to 15% in Income Bonds. The owners of the property also own $2,000,000 principal amount of Refunding and Improvement 6s of 1974, whose treatment will be later discussed. The owners of these bonds, desirous of composing differences between the other classes of bondholders to the greatest extent possible, are willing as a part of this plan to surrender for cancellation the $2,000,000 Refunding and Improvement 6s of 1974 as a contribution by the stockholders to the bondholders, and to let the earnings on such bonds apply to increase the percentage of Income Bonds allocable to the D&RG Consols. Such handling will permit these bonds to be offered 15% in Income 4s, to which their position as to equipment liens would entitle them, and at the same time permit treatment of the Refunding and Improvement Bonds on the basis of the maximum equipment lien which the Debtor believes them to possess.

The remaining principal amount of these bonds, 60%, are offered First Preferred Stock, the next ranking security, together with capitalization of unpaid interest. In this, as in other instances, unpaid interest has been capitalized fully to the extent accrued prior to the date of trusteeship, and has been capitalized to the extent estimated to be earned subsequent to such date. This treatment is believed to be not only fair and equitable, but all that it is legally permissible to accord under the provisions of Section 77 of the Bankruptcy Act.

[fol. 453] *RGW Consols* 4s, 1949

Outstanding	$13,080,000	
Pledged—RFC	3,395,000	$16,475,000

Net earnings available for interest in 1935 were a deficit of $228,799 after including an allowance for the stock of the Utah Fuel Company which is subject to the lien of this mortgage. The bonds are, however, a second lien upon the mileage which is subject to the RGW Trust 4s of 1939, which showed a net income available for interest in 1935 of approximately $1,871,560. This second lien position will permit the issuance within the desired earnings ratio of 40% in First and Refunding 4s to the holders of these bonds, with the remaining 60% of their principal, plus unpaid interest, allocated in Income Bonds.

D&RGW Refunding and Improvements

5s, 1978	Outstanding		$12,000,000
	Pledged RFC	$4,385,000	
	Pledged Bank	6,096,000	10,481,000
			22,481,000
6s, 1974	Outstanding		2,000,000
			$24,481,000

The direct net income of these bonds available for interest in 1935 was $40,490. The bonds are also a second lien on equipment subject to equipment trusts; a second collateral lien on the earnings of the RGJ, and a third lien on the mileage subject to the RGW Trust 4s of 1939. Earnings flowing to the Refunding and Improvement Bonds from these liens permits the issuance of 12.99% in [fol. 454] First and Refunding 4s (bonds in the hands of the public are offered 15%), 40% in Income 4s, and 45% in First Preferred Stock, together with capitalization of unpaid interest in the last named security.

The $2,000,000 of 6s, 1974, secured by the same mortgage, owned by the present common stockholders of the Debtor, are to be canceled as part of this plan and the earnings thereon distributed to the bondholders as heretofore stated.

RFC Debt— $10,691,850

This debt is secured by a first lien on all of the outstanding securities of the subsidiary company which owns the Dotsero Cutoff, and by more than 99% of the capital stock of the D&SL, together with the following other securities:

RGW Consol 4s	$1,395,000
D&RG Consol 4s	783,000
Refunding and Improvement 4s	4,385,000
D&SL Income 6s	1,266,000

and several other minor items.

Although, as stated, the earnings on this collateral will not justify offering the RFC 100% in new First and Refunding 4s, it is believed that the Strategic importance of the Cutoff route to the consolidated company dictates such an offer from the point of view of practicality, and this offer is therefore made.

[fol. 462]. In the Matter of the Reorganization of the Denver and Rio Grande Western Railroad Company, Debtor

Before the Interstate Commerce Commission

Finance Docket No. 11,062

Before the District Court of the United States for the District of Colorado. Bankruptcy Docket No. 8669

The Denver and Rio Grande Western Railroad Company

The Denver and Salt Lake Western Railroad Company, The Denver and Salt Lake Railway Company, The Rio Grande Junction Railway Company, Goshen Valley Railroad Company

Plan of Reorganization and Unification

Effective Date, January 1, 1937.
Proposed by Insurance Group Committee.

[fol. 463] The Denver and Rio Grande Western Railroad Company

The Denver and Salt Lake Western Railroad Company, The Denver and Salt Lake Railway Company, The Rio Grande Junction Railway Company, Goshen Valley Railroad Company

Plan of Reorganization and Unification

I.

Introductory Statement

Insurance Group Committee (hereinafter sometimes called the Committee) is the representative of a group of mutual life insurance companies owning substantial amounts of underlying bonds of The Denver and Rio Grande Western Railroad Company (hereinafter sometimes called the Denver) and of The Rio Grande Junction Railway Company (hereinafter sometimes called the Junction). The members of the Committee are George S. Van Schaick, Chairman; Jacob A. Barbey, Homer M. Chapin, Harry C. Hagerty,

In consideration of the offer of First and Refunding 4s for the entire amount of its debt, the RFC would agree as [fol. 455] part of the plan to underwrite the refunding of the $1,500,000 First Mortgage 4s of the D&SL in new First and Refunding 4s at 101 and the refunding of $9,734,000 Income 6s of the D&SL outstanding in the hands of the public in new First and Refunding 4s at 102.

These operations, together with an offer of Income 4s for the small amount of remaining outstanding capital stock of the D&SL, would result in the retirement of all of the securities of that company and their replacement by securities of the new consolidated company.

RCC Debt— $328,000

Based strictly on the collateral behind this loan, and valuing the balance due on the company's distributive share in the Marshalling and Distributing Fund at 60c on the dollar in First and Refunding 4s, an offer is made as follows:

Western Division 3½s	$66,000
First and Refunding 4s	179,000
Income 4s	83,000
	$328,000

Bank Debt— $1,500,000

For this debt, which is owed to the Chase National Bank, it is proposed to offer Ten-Year Collateral Notes covering the face amount of debt, plus capitalizable interest, secured by those securities of the new company issuable for the collateral securing the present loan if exchanged under the provisions of the plan. This loan is secured by $6,096,000 [fol. 456] principal amount of Refunding and Improvement 5s of 1978. As the plan stands at present, the Ten-Year Notes offered to the Chase Bank would be secured by $792,000 principal amount of First and Refunding 4s, by $2,479,000 principal amount of Income 4s, and by $2,825,000 par value of First Preferred Stock.

D&RGW General 5s, 1955— $29,808,000

These bonds are offered the next ranking security, namely, Participating Preferred Stock, for 100% of their principal, plus capitalizable interest at the rate of one share of stock

for each $100 of obligation capitalized. Unpaid accumulations on these bonds during the five year period 1924-1929 are not capitalized inasmuch as by the terms of the mortgage they do not have to be paid if remaining unpaid at the maturity of the bonds.

General Creditors—

It is proposed that unsecured general creditors be offered Participating Preferred Stock at the rate of one share of stock for each $100 of claim. Should any general creditors prove to have claims secured to such an extent as to justify better treatment than that proposed for unsecured creditors, it is proposed that the Debtor company as reorganization manager be granted authority to allocate other securities in settlement of such claims, subject to the approval of the Interstate Commerce Commission.

Preferred Stock— $16,445,600

Present Preferred stock is proposed to be exchanged for new Participating Preferred Stock on the basis of one [fol. 457] new share of Preferred for each two shares of existing preferred.

Common Stock— 300,000 sh.

The Missouri Pacific Railroad Company and The Western Pacific Railroad Corporation are the two present common stockholders. On the east, the Missouri Pacific is the most important interchange for freight business, its interchange more than equalling the combined interchange of the two next largest connecting lines. On the west, the Western Pacific Railroad Company, controlled by the Western Pacific Railroad Corporation, is also by far the most important connection from an interchange point of view. In view of this situation the Debtor believes it essential that the definite interest of these controlling carriers be retained. Under this plan each is offered 100,000 shares of new common for 150,000 shares of old common and $1,000,000 principal amount of Refunding and Improvements 6s of 1974 presently held. In addition, each of the present common stockholders will agree to purchase $1,500,000 of new First and Refunding Series A 4% Bonds at par and accrued interest.

X

Execution of Plan

Subject to any requirements of law and the requisite approval of the Court and the Interstate Commerce Commission, the principal Debtor company shall have, in ac- [fols. 458-460] cordance with the authority granted by Section 77, of the Bankruptcy Act, full and discretionary powers to make and enter into all such arrangements and to do all such things as it may deem necessary or advisable in order to promulgate, consummate, execute and make fully effective any plan of reorganization recommended, approved and certified by the Interstate Commerce Commission and confirmed by the Court. The expenses of reorganization shall be paid out of the new capital provided by this plan of reorganization.

July 28, 1936.

Fred P. Mayward, Carrol M. Shanks and Frederick W. Walker. The principal amounts of the bonds owned by the institutions so represented are as follows:

Rio Grande Junction Railway First Mortgage 5's (hereinafter sometimes called the Junction Bonds)	$698,000
Rio Grande Western First Trust 4's (hereinafter sometimes called First Trust 4's)	4,601,000
Rio Grande Western Consolidated 4's (hereinafter sometimes called the Western Consols)	4,500,000
Denver and Rio Grande Consolidated 4's (hereinafter sometimes called the Eastern Consol 4's or, collectively with the Eastern Consol 4½'s, the Eastern Consols)	5,009,000
Denver and Rio Grande Consolidated 4½'s (hereinafter sometimes called the Eastern Consol 4½'s, or, collectively with the Eastern Consol 4's, the Eastern Consols)	1,316,000
Total	$15,874,000

[fol. 464] On November 1, 1935, the Denver and The Denver and Salt Lake Western Railroad Company (hereinafter sometimes called the Salt Lake Western) filed petitions for reorganization under Section 77 of the Bankruptcy Act in the District Court of the United States for the District of Colorado. Such petitions were approved as properly filed, and Trustees appointed by that Court have subsequently administered the properties of those Companies. In July, 1936, a plan of consolidation and reorganization embracing the Denver, the Salt Lake Western, The Denver and Salt Lake Railway Company (hereinafter sometimes called the Salt Lake), the Junction and Goshen Valley Railroad Company was filed in behalf of the Denver.

For a substantial period prior to that time the Committee (and before its formal organization, representatives of some of its member institutions) had been conducting discussions and negotiations with representatives of the Denver in an effort to develop a sound and just plan of reorganization which would be acceptable to all interests involved. Various changes in the characteristics and terms of its intended plan were made by the Denver in response to positions taken by the Committee. Further changes in said proposed plan were recommended by the Denver to the Interstate Commerce Commission (hereinafter sometimes called the Commission) during the course of the hearings which have been held. Even after all such changes, however, the plan of the Denver does not, in the view of the Committee, [fol. 465] afford due recognition to the rights of the various classes of bondholders and is neither fair nor equitable, but discriminates unfairly in favor, among others, of the common stockholders under whose supervision said plan was

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY

THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY
THE DENVER AND SALT LAKE RAILWAY COMPANY
THE RIO GRANDE JUNCTION RAILWAY COMPANY
GOSHEN VALLEY RAILROAD COMPANY

Exhibit B

PROPOSED PLAN OF CONSOLIDATION AND REORGANIZATION AS OF JANUARY 1, 1937

EXISTING CAPITALIZATION	Amount	Undisturbed	Western Division First Mortgage Bonds Series A—3½% Maturity: 40 Years		First and Refunding Mortgage Bonds Series A—4% Maturity: 60 Years		General Income Mortgage Bonds Series A—4% Maturity: 75 Years		First Preferred Stock 4½% Par Value $100 per Share		Participating Preferred Stock Par Value $1— $5 Dividends (No. Shares)
The Denver and Rio Grande Western Railroad Company:											
Equipment Trust Certificates	$ 1,805,000	$ 1,805,000	$		$		$		$		
R. G. J. 5s, 1939, Principal	2,000,000		(Note A)	2,000,000							
Unpaid Interest	158,333		(7.92%)	158,333							
R. G. W. Trust 4s, 1939, Principal	15,190,000		(Note B)	15,190,000							
Unpaid Interest	1,215,200		(8.00%)	1,215,200							
D. & R. G. Consol. 4s, 1936, Principal	34,125,000		(10%)	3,412,500	(15%)	5,118,750	(15%)	5,118,750	(60%)	20,475,000	
Unpaid Interest	3,412,500								(6.66%)	2,274,140	
D. & R. G. Consol. 4½s, 1936, Principal	6,382,000		(10%)	638,200	(15%)	957,300	(15%)	957,300	(60%)	3,829,200	
Unpaid Interest	717,975								(7.50%)	478,469	
R. G. W. Consol. 4s, 1949, Principal	15,080,000				(40%)	6,032,000	(60%)	9,048,000			
Unpaid Interest	1,357,200						(8.25%)	1,244,836			
D. & R. G. W. Ref. and Impr. 5s, 1978, Principal	12,000,000				(15%)	1,800,000	(40%)	4,800,000	(45%)	5,400,000	
Unpaid Interest	1,350,000								(6.27%)	751,809	
Reconstruction Finance Corp. Debt, 4%, Principal	10,691,850					10,691,850					
Unpaid Interest	626,108					391,150					
The Railroad Credit Corp. Debt, 1½% (Est.)	328,000			66,000	(Note C)	179,000		83,000			
Bank Debt, 5%, Principal (Note D)	1,500,000					792,000		708,000			
Unpaid Interest	93,948							58,000			
D. & R. G. W. General 5s, 1955, Principal	29,808,000										298,08
Unpaid Interest	12,544,200										33,53
Preferred Stock	16,445,600								(50%)	82,22	
D. & R. G. W. Ref. and Impr. 6s, 1974, Principal	2,000,000										
Unpaid Interest	270,000										
Common Stock	Shs 300,000										
Total Capitalization		1,805,000		22,680,233		25,962,050		22,017,886		33,208,618	413,84
Charges		68,408		793,808		1,038,482		880,715		1,194,388	$ 2,069,21
Charges—Cumulative		68,408		862,216		1,900,698		2,781,413		4,275,801	$ 6,345,01
The Denver and Salt Lake Railway Company:											
First 4s, 1960, Principal	1,500,000				(101%)	1,515,000					
Income 6s, 1960 (with public), Principal	9,734,000				(102%)	9,928,680					
Stock (with public)	Shs 460							46,000			
Total Capitalization						11,443,680		46,000			
Charges						457,747		1,840			
Charges—Cumulative						457,747		459,587		459,587	$ 459,58
The Denver and Rio Grande Western Railroad Company—The Denver and Salt Lake Railway Company											
Grand Total Capitalization		1,805,000		22,680,233		37,405,730		22,063,886		33,208,618	413,84
Charges		68,408		793,808		1,496,229		882,555		1,194,388	$ 2,069,21
Charges—Cumulative		68,408		862,216		2,358,445		3,241,000		4,435,388	$ 6,501,59

LROAD COMPANY
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Exhibit B

S OF JANUARY 1, 1937

ng rs	General Income Mortgage Bonds Series A—4% Maturity: 75 Years		First Preferred Stock 4½% Par Value $100 per Share		Participating Preferred Stock Par Value $1— $5 Dividends (No. Shares)		Common Stock Par Value $1 per Share (No. Shares)
	$		$				
18,750	(15%)	5,118,750	(60%)	20,475,000			
			(6.66%)	2,274,140			
57,300	(15%)	957,300	(60%)	3,829,200			
			(7.50%)	478,469			
82,000	(60%)	9,018,000					
	(8.25%)	1,244,836					
00,000	(40%)	4,800,000	(45%)	5,400,000			
			(6.27%)	751,809			
01,850							
01,150							
79,000		83,000					
82,000		708,000					
		58,000					
						298,080	
						33,534	
					(50%)	82,228	
							200,000
2,050		22,017,886		33,208,618		413,842	200,000
8,482		880,715		1,494,388	$	2,039,210	
0,698		2,781,413		4,275,801	$	6,315,011	
5,000							
8,680							
		46,000					
3,680		46,000					
7,747		1,840					
7,747		459,587		459,587	$	459,587	

proposed. It has, therefore, seemed to the Committee that it should propose a plan which would be fair to all interests and provide for equitable participation of the various classes of creditors and stockholders, while making provision for the future of the companies involved which would best promote the earning power and financial strength of the several properties and their ability to continue and improve the public service rendered by them. To that end this Plan of Reorganization and Unification (hereinafter sometimes called the Plan) is being filed by the Committee with the Commission and the Court.

The statements and figures herein contained with respect to the capitalization and earnings of the several companies embraced within the Plan have been taken from information supplied by the Denver, but no estimate, statement, explanation or suggestion contained in the Plan, or in any circular that may hereafter be issued by or under the authority of the Committee or of the Reorganization Committee hereinafter named, is intended or is to be accepted as a representation.

[fol. 368]

II

Capitalization Outstanding as of January 1, 1937

(Including Unpaid Interest)

		Amount	Fixed Annual Interest
The Denver and Rio Grande Western Railroad Company:			
Equipment Trusts	$1,805,000	$1,805,000	$68,408
Rio Grande Junction First Mortgage 5's due 1939 (Junction Bonds)			
Principal	2,000,000		100,000
Unpaid Interest	158,333		
Total		2,158,333	
Rio Grande Western First Trust 4's of 1939 (First Trust 4's)			
Principal	15,190,000		607,600
Unpaid Interest	1,215,200		
Total		16,405,200	
(In addition $10,000 principal amount of such bonds are pledged with Reconstruction Finance Corporation)			
Denver and Rio Grande Consolidated 4's due 1936 (Eastern Consol 4's)			
Principal	34,125,000		1,365,000
Unpaid interest	3,412,500		
Total		37,537,500	

[fol. 467]

		Amount	Fixed Annual Interest
(In addition, $783,000 principal amount of such bonds are pledged with Reconstruction Finance Corporation and $662,000 principal amount with The Railroad Credit Corporation)			
Denver and Rio Grande Consolidated 4½'s due 1936 (Eastern Consol 4½'s)			
Principal	6,382,000		287,190
Unpaid interest	717,975		
Total		7,099,975	
Rio Grande Western Consolidated 4's due 1949 (Western Consols)			
Principal	$15,080,000		$603,200
Unpaid interest	1,357,200		
Total		$16,437,200	
(In addition $1,395,000 principal amount of such bonds are pledged with Reconstruction Finance Corporation)			
Denver and Rio Grande Western Refunding and Improvement 5's due 1978 (hereinafter sometimes called the R&I's or R&I 5's)			
Principal	12,000,000		600,000
Unpaid interest	1,350,000		
Total		13,350,000	

[fol. 468]

		Amount	Fixed Annual Interest
(In addition, $6,096,000 principal amount of such bonds are pledged with The Chase National Bank of the City of New York and $4,385,000 principal amount with Reconstruction Finance Corporation)			
Denver and Rio Grande Western Refunding and Improvement 6's due 1974 (hereinafter sometimes called the R&I 6's)			
Principal	2,000,000		120,000
Unpaid interest	270,000		
Total		2,270,000	
Denver and Rio Grande Western General Mortgage 5's due 1955 (hereinafter sometimes called the General Mortgage Bonds)			
Principal	29,808,000		1,490,400
Unpaid interest	12,544,200[1]		
Total		42,352,200	
Notes (4%) to Reconstruction Finance Corporation (hereinafter called RFC)			
Principal	10,691,850		427,674
Unpaid interest	626,108		
Total		11,317,958	
Notes (1½%) to The Railroad Credit Corporation (hereinafter called RCC)	$297,409	$297,409	$4,920
Notes (5%) to The Chase National Bank of the City of New York (hereinafter called the Chase Bank)			
Principal	1,500,000		75,000
Unpaid interest	93,948		
Total		1,593,948	

[1] $7,452,000 of this amount represents interest for the five year period ending February 1, 1929, during which time the payment of interest was contingent.

[fol. 469]

		Amount	Fixed Annual Interest
Total Funded Debt (excluding pledged bonds) and Notes		$152,624,723	$5,749,392
Preferred Stock—Par Value	$16,445,600		
Common Stock—Shares	300,000		
The Denver and Salt Lake Railway Company:			
First Mortgage 4's due 1950		$1,500,000	$60,000
Income Mortgage 6's due 1960		9,734,000	584,040[2]
(In addition, $1,266,000 principal amount of such bonds are owned by the Denver and pledged with RFC)			
Common Stock—Shares	50,000		
(460 of these shares are outstanding in the hands of the public and the residue are owned by the Denver and pledged with RFC)			
The Denver and Salt Lake Western Railroad Company:			
Common Stock—Shares	36,310[3]		
System Total Funded Debt (excluding pledged bonds) and Notes		$163,858,723	$6,393,432[2]

[2] Interest of $584,040 on the Salt Lake Income Bonds (which is included in the system total) is contingent.

[3] All such shares are owned by the Denver and pledged with RFC. In addition the Salt Lake Western is obligated on notes to RFC, which are included in the aforesaid indebtedness by the Denver to RFC.

GENERAL NOTE: There are likewise outstanding $2,217,000 principal amount of The Northwestern Terminal Railroad Company First Mortgage Income 5's; the properties of such company are operated by the Salt Lake under lease, and interest on its bonds may become a fixed charge by way of rental in the event of a merger or consolidation of the Salt Lake and the Denver. Rental under the lease of the Moffat Tunnel held by the Salt Lake includes a part of the principal and interest of the bonds issued to finance the construction of such tunnel. In addition, the Denver is liable with respect to obligations of terminal companies at Denver and Salt Lake City.

[fol. 470]

III

Earnings of the Properties

The statements filed by the Denver with the Interstate Commerce Commission indicate that the Total Operating Revenues and Net Available for Interest of the companies embraced within the Plan on a consolidated basis for the years 1930-35, inclusive, were (after the correction stated below) as follows:

Year	Total Operating Revenues	Net Available for Interest
1930	$32,944,819	$8,060,527
1931	25,787,653	6,139,950
1932	19,476,090	3,560,344
1933	18,770,125	3,930,497
1934	20,866,856	3,477,744
1935	23,179,112	3,459,100

In the above table Net Available for Interest for the year 1935 has been corrected by the elimination of a charge made by the Denver in said statements in the sum of $263,884 purporting to represent "Federal Retirement Act Contributions". This correction has been made because of the fact that no such contributions were required in that year.[1]

The statements so filed by the Debtor do not show the earnings of the consolidated properties for the year 1936. The available reports show that the Total Operating Revenues of the properties embraced in the Plan upon a consolidated basis for the year 1936 amount to $28,456,258. [fol 471] Certain of the operating expenses of the properties were distorted in that year by large expenditures being made by the Trustees of the Denver for improvements. Applying the average operating ratio for the ten year period 1926-1935, inclusive, to the Total Operating Revenues of the Denver for the year 1936 and taking the other items in the income accounts as reported for the year 1936 would give a net available for interest in that year of $4,557,748 on a consolidated basis.

The foregoing figures produce an average Net Available for Interest for the four years 1932-1935 of $3,606,921; for the five years 1932-1936 of $3,797,086; for the two years 1935-1936 (the only two calendar years of operation since the opening of the Dotsero Cut-Off) of $4,008,424.

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[1] It would appear that this sum is composed of $175,625 charged to operations in 1934 and credited to profit and loss in 1935 and $88,259 charged to operations in the first three months of 1935 and credited to operations in April, 1935.

pari passu with the lien of the new Income Mortgage except as in the new Income Mortgage otherwise expressly provided unless the creation of such mortgage or lien be consented to by the holders of all outstanding new Income Bonds.

Available Net Income and Capital Fund

The First Mortgage and the Income Mortgage shall make appropriate provision for the determination and application of Available Net Income and a Capital Fund as follows:

Available Net Income shall be determined for each period of six months ending June 30th or December 31st (hereinafter called Income Periods) beginning with the Income Period ending June 30, 1937.

Available Net Income for each Income Period shall equal the remainder left after deducting from the income of the New Company arising from the properties subject to the lien of the New Income Mortgage and from the properties [fol. 485] or systems acquired by the New Company under the Plan which is available for fixed charges for such Income Period (determined in accordance with the accounting rules at the time in force of the Commission or other analogous Federal authority having jurisdiction at the time, or, to the extent not covered by such accounting rules, in accordance with sound accounting practice) such part of the following amounts as arise in the operation of, or are incident to, the aforesaid properties, namely:

(a) All fixed charges (determined in accordance with such accounting rules or practice) of the New Company accrued during such Income Period; provided, however, that if in any Income Period the New Company shall fail to earn such fixed charges, the amount of such deficit may in the discretion of the Board of Directors of the New Company (and shall in the event that funds shall have been borrowed because of such deficit to pay such fixed charges) be paid out of income for the next ensuing Income Period or Periods before determining Available Net Income, and any income so deducted before determining Available Net Income shall be first used to retire any indebtedness that may have been incurred for the purpose of paying such fixed charges;

(b) All other charges properly deductible from such income in determining income after fixed charges under such accounting rules or practice, but excluding contingent interest and sinking fund requirements hereinafter provided for; and

(c) The sum, subject to the proviso set out in paragraph [fol. 486] number (5) next hereinbelow, of 2½% of total railway operating revenues (determined in accordance with such accounting rules or practice) of the New Company for such Income Period subject to a maximum limit of $375,000, which sum shall constitute the Capital Fund and be disposed of as hereinafter set forth. Any amount by which such income in any Income Period shall be inadequate to provide for the Capital Fund shall accumulate and be carried forward into the next succeeding one Income Period, but not beyond.

Available Net Income for each Income Period shall be applied to the following purposes and in the following order:

(1) All Available Net Income shall, to the extent required and subject to the provision hereinabove made for payment in even multiples of ¼% and postponement of fractional surplus, be applied to the payment on October 1st and April 1st in each year, beginning October 1, 1937, of interest on the then outstanding new Income Mortgage Bonds (excluding bonds then held in the sinking fund under the new Income Mortgage) accruing during the Income Period ending on the next preceding June 30th or December 31st, respectively, and to the payment of any unpaid accumulated interest on said bonds.

(2) Any then remaining Available Net Income shall be applied until all the new Income Bonds shall have been retired, on October 1st and April 1st in each year, beginning on October 1, 1937, to a sinking fund for such bonds [fol. 487] in an amount up to, but not exceeding, in respect of any Income Period, one-eighth of 1% of the total principal amount of Income Bonds to be issued in the reorganization plus an amount equal to interest on Income Bonds theretofore purchased or redeemed for the sinking fund, calculated at the rate paid (pursuant to the foregoing clause (1)) in respect of such Income Period, including accumulations, upon outstanding Income Bonds. Any

amount by which Available Net Income remaining for such purpose is inadequate to pay the full amount of such instalment of sinking fund shall be cumulated within the limits hereinabove stated and added to the instalment payable in the next ensuing Income Period or Periods.

(3) Any then remaining Available Net Income may be applied to any proper corporate purpose of the New Company (except dividends on the new Common Stock), including, if, and to the extent that, such dividends shall be declared by the Board of Directors of the New Company, the payment on April 1st of each year, beginning April 1, 1938, of dividends upon the new Preferred Stock in respect of the two Income Periods ending on the next preceding December 31st, to the extent not theretofore paid, and of any accrued and unpaid cumulative dividends on the new Preferred Stock and, if and to the extent so declared, to the payment on October 1st in each year, beginning on October 1, 1937, of interim dividends on the new Preferred Stock in respect of the Income Period ending on the next preceding June 30th, and of any accrued and unpaid cumulative dividends.

[fol. 488] (4) Any then remaining Available Net Income may be applied to any proper corporate purpose of the New Company, including (but only after all accrued and unpaid dividends, including accrued and unpaid cumulative dividends, on the new Preferred Stock to the next preceding June 30th or December 31st, as the case may be, shall have been paid or declared and set apart for payment) dividends on the new Common Stock.

(5) The above provisions for the deduction of the Capital Fund from the income of the New Company available for fixed charges are subject to the following provisos: If the New Company shall establish and maintain, in such manner as may be permitted or required by law or lawful regulation, an operating expense account for depreciation of its roadway and structures, then (a) the Capital Fund shall be paid from the reserve for depreciation on roadway and structures so credited in respect of the applicable Income Period to the extent that the amount so credited to said depreciation reserve shall be adequate therefor; (b) to that extent the foregoing provisions for the deduction of the Capital Fund shall cease to be operative; and (c) the New

Company shall not be entitled to withdraw any moneys from the Capital Fund until it shall have expended in the current calendar year for additions and betterments properly chargeable to capital account under said accounting rules or practice more than the amount by which its charge for depreciation of roadway and structures in such year [fol. 489] less cash expenditures incurred in the making of retirements properly charged to the depreciation reserve so credited exceeds the total paid into the Capital Fund in such year and then only to the extent of such excess.

(6) Available Net Income for any period after January 1, 1937, until the New Company comes into ownership and possession of the properties of the companies embraced in the Plan (or of their Trustees in Bankruptcy) shall be computed as if the New Company had come into such ownership and possession on January 1, 1937, and had issued, as of that date, the new securities issuable under the Plan.

The Capital Fund shall be paid to the Trustee under the new First Mortgage on October 1st and April 1st of each year and shall (subject to the proviso in the next preceding paragraph numbered (5)) be withdrawable by the New Company at any time before the next Capital Fund payment date to reimburse it for, or to provide for:

(a) All of the cost payable in cash of additions or betterments to the mortgaged property, including equipment, which are properly chargeable to capital account under said accounting rules or practice, made or to be made in the calendar year within which such payment into the Capital Fund is due, and not previously certified or thereafter to be certified to the Trustee under the new First Mortgage as the basis, in whole or in part, for the issuance of additional new First Mortgage Bonds, or the release of mortgaged property or the withdrawal of cash held by such Trustee, [fol. 490] and further provided that no expenditures so used as a basis for the withdrawal of any moneys from the Capital Fund shall be made the basis for the issuance by the New Company of any form of indebtedness or stock ranking prior to or on a parity with the new Preferred Stock of Series A; and

(b) All of the amount by which the Unfundable Purchase Price (as hereinafter defined) for new equipment exceeds Equipment Depreciation Surplus (as hereinafter defined).

In the case of equipment acquired under equipment trust obligations, the Unfundable Purchase Price shall equal the initial or down payment for such equipment. In the case of equipment acquired and paid for by the withdrawal of deposited cash under the new First Mortgage, the Unfundable Purchase Price shall equal that part of the purchase price not so withdrawable. Equipment Depreciation Surplus shall equal the remainder determined by deducting (1) the total instalments of principal of equipment trust obligations or other obligations for the deferred or serial payment of the purchase price for equipment and instalments of Equipment Sinking Fund paid out of equipment depreciation as hereinabove provided in the two next preceding Income Periods from (2) the total charges to operating expenses in such two Income Periods for depreciation of equipment. Such withdrawals from the Capital Fund shall be permitted only on the basis of such payments for equipment made or to be made in the calendar year in which the payment of such moneys into the Capital Fund was due.

[fol. 491] Any moneys not withdrawn from the Capital Fund by the New Company as aforesaid shall be accumulated in the hands of the Trustee under the new First Mortgage (subject to investment in United States Government bonds or treasury certificates) until the aggregate sum so accumulated shall equal interest requirements for a period of one year on the bonds then outstanding under the new First Mortgage; moneys so accumulated and held by said Trustee shall be designated as the Interest Reserve Fund and shall be withdrawable by the New Company only for the purpose of paying interest on bonds outstanding under the new First Mortgage in a year or years in which the net earnings of the New Company available for the payment of interest on said bonds shall be inadequate for the payment of such interest, and only to the extent of such inadequacy.

When moneys shall have accumulated in the Interest Reserve Fund to the full extent of interest requirements for a period of one year on the bonds at the time outstanding under the new First Mortgage, any moneys not withdrawn from the Capital Fund by the New Company as aforesaid shall, so long as any new Income Mortgage Bonds shall be outstanding, be paid to the Trustee under the new Income Mortgage as an additional payment into the sinking fund thereunder; and, when all the new Income Mort-

gage Bonds shall have ceased to be outstanding, be applied by the Trustee under the new First Mortgage to the re-
[fol. 492] tirement of the First Mortgage Bonds of Series A so long as any thereof shall remain outstanding and thereafter to the retirement of any First Mortgage Bonds issued in reorganization other than Series A or Series B, so long as any thereof shall remain outstanding, and thereafter to the retirement of the First Mortgage Bonds of Series B, so long as any thereof shall remain outstanding, by purchase, at the lowest prices obtainable, at public or private sale or upon calls for tender, and to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of said bonds, in any case at not exceeding the redemption price of said bonds. All First Mortgage Bonds so purchased or redeemed shall be cancelled and retired and no bonds shall be issued in lieu thereof. The New Company shall pay from its general funds all accrued and payable interest on any Income Mortgage Bonds or First Mortgage Bonds purchased or redeemed by the Capital Fund.

When there shall remain outstanding no Income Mortgage Bonds and no First Mortgage Bonds issued under the Plan, these provisions for the determination and application of Available Net Income and the Capital Fund shall cease to be effective.

Contingent Ten Year Collateral Notes

The Contingent Ten Year Collateral Notes will be dated January 1, 1937, and will mature January 1, 1947, subject, however, to renewal or renewals from time to time at the option of the New Company for further periods of ten
[fol. 493] years each until retired in the manner to be set forth in the agreement securing such Notes. Such Notes will bear interest at the rate of 4% per annum, payable semi-annually on October 1st and April 1st of each year, beginning October 1, 1937, but such interest will be contingent on, and payment thereof shall be limited to, the total of the interest and dividends paid by the New Company on the collateral securing such Notes. The interest will be cumulative to the maximum amount at any one time of 22½% (whether for consecutive or non-consecutive Income Periods). Any interest and/or dividends paid upon the pledged collateral in excess of interest require-

[fol. 472] IV

Proposed Capitalization of the New Company

The proposed capitalization of the New Company is as follows:

Summary	Presently Issued	Charges
Undisturbed Equipment Trusts	$1,805,000	$68,408[1]
First Mortgage Bonds, Series A	18,563,533	742,541[2]
First Mortgage Bonds, Series B	46,468,084[3]	1,858,724
Total Annual Fixed Charges		2,669,673[3]
Capital Fund		750,000[4]
Income Mortgage Bonds	28,052,011	1,262,340
Total Annual Charges (fixed and contingent) and Capital Fund		4,682,013
Income Mortgage Sinking Fund		70,130
Preferred Stock (par value)	31,434,986	1,571,749
Total Annual Charges, Capital Fund, Sinking Fund and Preferred Dividend Requirements		6,323,892
Common Stock—Class A (shares)	349,002	
Series A Warrants to purchase voting trust certificates for shares of Common Stock, Class A (see below) calling for (shares)	164,456	
Series B Warrants to purchase voting trust certificates for shares of Common Stock, Class B (see below) calling for (shares)	200,000	
Option to purchase shares of Common Stock, Class B (see below) calling for (shares)	200,000	

[1] Since January 1, 1937, the Trustees of the Denver have issued $2,175,000 principal amount of Equipment Trust Certificates, which will also be assumed by the New Company.

[2] Interest computed at 4% but may be increased to not exceeding 4½% as provided hereinbelow.

[3] Excludes provision for $6,000,000 principal amount of new First Mortgage Bonds reserved to be issued if and to the extent necessary to retire Trustees' Certificates, pay reorganization expenses and provide working capital. The amount of Series B Bonds may possibly be increased through conversion of the new Income Mortgage Bonds to be issued to RFC, as provided hereinbelow.

[4] Maximum amount; 2½% of total railway operating revenues, but not to exceed $750,000 per year.

GENERAL NOTE: Certain of the above First Mortgage Bonds, Income Mortgage Bonds and Preferred Stock are, as provided hereinbelow, to be pledged as collateral for Contingent Ten Year Collateral Notes. All references in the Plan to securities to become outstanding under the Plan include such collateral. If RFC is not paid in cash, certain additional amounts of such bonds and stock will be issued and pledged as collateral.

[fol. 473] *New First Mortgage Bonds*

The new First Mortgage will constitute a first lien, subject only to the lien of equipment trust obligations, on (1) all property owned by the companies embraced within the Plan or their Trustees in Bankruptcy as such, at the time of the effectuation of the Plan, including securities, equipment and the equity in such equipment as may be subject to equipment trust obligations, but excluding the narrow gauge railway lines of the Denver and equipment

and property essential to the operation thereof; (2) the capital stock of Utah Fuel Company; (3) all property acquired by the New Company after the date of the new First Mortgage for use on or in connection with the mortgaged property, subject only to such encumbrances or purchase money liens as may exist or be created at the time of acquisition. So far as the Reorganization Committee may deem practicable, such lien shall be in the form of direct mortgage, but it may take the form of the pledge or assignment of securities of a corporation or corporations owning property to which the lien is intended to extend.

Such new First Mortgage will contain a covenant that, to the extent permitted by law or lawful regulation, the New Company shall in each Income Period as hereinafter defined charge to operating expenses an amount for depreciation of equipment at least equal to the total amount of all instalments of principal of equipment trust obligations or other obligations for the deferred or serial pay- [fol. 474] ment of the purchase price for equipment maturing in such Income Period plus an amount equal to the instalments payable in such Income Period of the Equipment Sinking Fund (as hereinafter defined) provided for new First Mortgage Bonds and, out of the depreciation reserve so credited, will pay all such instalments as they become payable.

Such new First Mortgage will contain a covenant that the New Company will, at all times, keep the mortgaged property supplied with such amount of motive power, rolling stock and equipment (upon which the new First Mortgage shall constitute a paramount lien subject only to such purchase money liens as may be permitted by the terms thereof), and maintain the same in such condition, as may be necessary for the efficient and economical operation of the mortgaged property.

The new First Mortgage Bonds may be issued in series, all equally secured as to principal and interest, which may differ as to date of maturity, interest rate, redemption price and other terms. Additional bonds other than those to be issued under the Plan may be issued under the First Mortgage, without limit as to amount; or within such limit as may be specified in the First Mortgage, on such bases (including the refunding of debt and the deposit of cash) as shall be prescribed therein, provided that: (1) bonds may be issued on the basis of additional property (includ-

ing new equipment free from any other lien) and additions and betterments only to the extent of 75% (less prior lien debt) of the net amount of such additional property [fol. 475] or additions and betterments, computed on the basis of cost (including prior lien debt) thereof or value thereof to the New Company, whichever may be less; (2) bonds may not be issued on the basis of additional property of any kind or additions and betterments or on the basis of deposited cash unless the income of the New Company available for fixed charges in a period of twelve consecutive calendar months within the fifteen calendar months immediately preceding the date of authentication and delivery (determined in accordance with the accounting rules of the Commission or other analogous Federal authority having jurisdiction at the time, or, to the extent not governed by such accounting rules, in accordance with sound accounting practice) equals or exceeds one and one-half times the fixed charges, determined in accordance with such accounting rules or practice, of the New Company, including interest on the bonds then applied for; (3) additional property (with the exception as to equipment hereinbelow specifically provided) or additions and betterments acquired by the use of the Capital Fund hereinafter provided for shall not be eligible as a basis, in whole or in part, for the issuance of bonds and (4) no additional bonds of Series A other than those to be issued under the Plan may be issued and no bonds may be issued of any series having a maturity on or before the maturity of the bonds of Series A except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition. Whenever any bonds shall be [fol. 476] issued or deposited cash withdrawn on the basis of the acquisition of new equipment or to provide cash for such acquisition, an Equipment Sinking Fund shall be established under which the New Company will pay in cash to the Trustee under the new First Mortgage on January 1st and July 1st of each year an instalment of sinking fund equal to the quotient determined by dividing the principal amount of such bonds or the amount of cash so withdrawn by twice the number of years embraced in the original effective service life of such equipment (in no case to exceed fifteen) less the time elapsed since the acquisition of such equipment. Moneys held in such sinking fund shall be applied to the retirement of such bonds, or of any new

First Mortgage Bonds as to be specified in the new First Mortgage, by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders or, to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. The new First Mortgage may provide a sinking fund with respect to additional bonds that may be issued thereunder other than those to be issued under the Plan and other than those that may be issued on the basis of the acquisition of new equipment as aforesaid. No bonds shall be issued on the basis of the acquisition of equipment under equipment trust obligations or any obligations for the deferred or serial payment of purchase price, or on the basis of the retirement of any such obligations.

[fol. 477] The new First Mortgage shall provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof and of any or all supplements thereto and of the rights and obligations of the New Company thereunder and of the holders of the bonds at any time by the concurrent action of the New Company and of the holders of not less than two-thirds in aggregate principal amount of the bonds then outstanding affected by such change or modification; provided that no such change or modification shall (a) alter or impair the obligation of the New Company to pay the principal or interest of any bond at the time and place and at the rate and in the currency provided therein without the consent of the holder of such bond, or (b) permit the creation by the New Company of any mortgage or lien in the nature of a mortgage ranking prior to or *pari passu* with the lien of the new First Mortgage except as in the new First Mortgage otherwise expressly provided unless the creation of such mortgage or lien be consented to by the holders of all outstanding bonds.

It is proposed that the bonds of Series A to be issued under the Plan be dated January 1, 1937, mature January 1, 1962, and bear interest at the rate of 4% per annum, payable semi-annually. Such proposal is, however, subject to the controlling policy that such bonds be given terms and characteristics appropriate to assure to such bonds at the time of issuance a market value equal, as nearly as may be, to their principal amount; to that end the Reorganization [fol. 478] Committee shall have the power at any time before the issuance of such bonds, subject to the approval

of the Commission, to reduce the term of such bonds to not less than ten years, increase the rate of interest on such bonds to not exceeding 4½%, provide for their issuance as collateral trust bonds secured by not exceeding 115% of new First Mortgage Bonds, or adopt any combination of such provisions as in the judgment of the Reorganization Committee may be best suited to the effectuation of said policy. No such change shall be deemed a modification of the Plan.

Each bond of Series A shall be convertible at any time on or before fifteen days prior to the date as of which such bond shall have been called for redemption into a bond of Series B having the same principal amount, with appropriate adjustment for accrued and unpaid interest to the date of conversion. The bonds of Series A shall be redeemable in whole or in part at any time on sixty days' notice by publication, at their principal amount and accrued interest.

The bonds of Series B to be issued under the Plan shall be dated January 1, 1937, shall mature January 1, 1977, shall bear interest at the rate of 4% per annum, payable semi-annually, and shall be redeemable in whole or in part at any time upon thirty days' notice by publication, at their principal amount and accrued interest, plus a premium of 5% of their principal amount if redeemed on or before January 1, 1942, 3½% of their principal amount if re- [fol. 479] deemed on or before January 1, 1947, 2½% if redeemed on or before January 1, 1952, and 1% if redeemed on or before January 1, 1972.

There shall also be issuable in or after reorganization $6,000,000 principal amount of new First Mortgage Bonds of Series B or some other series other than Series A. As many thereof as may be requisite shall be issued and sold at such price as may be approved by the Commission to provide funds to redeem all certificates then outstanding issued by the Trustees of the Denver or the Trustee of the Salt Lake Western (other than equipment trust certificates) and the residue shall be used to provide for reorganization expenses and working capital or held in the treasury of the New Company available for sale or pledge on such terms as may be approved by the Board of Directors of the New Company.

The bonds to be issued to provide for the refunding of the Salt Lake bonds, as stated below, shall also be of Series B or some other series other than Series A and shall be sold at such price as may be approved by the Commission.

New Income Mortgage Bonds

The new Income Mortgage will constitute a lien subject only to the lien of the First Mortgage and any lien that may at the time be prior to the lien of the First Mortgage, upon all property from time to time subject to the lien of the First Mortgage. Such mortgage will be closed at the [fol. 480] principal amount of bonds to be issued thereunder in the reorganization.

The new Income Mortgage bonds to be issued in the reorganization shall be dated January 1, 1937, shall mature January 1, 1987, and shall bear interest at the rate of 4½% per annum, payable semiannually. Such interest shall (within the limits of accumulation hereinafter specified) become absolutely due as a debt on its respective due dates of October 1st and April 1st in each year in respect of Income Periods ending the next preceding June 30th and December 31st, respectively. Interest on the new Income Mortgage Bonds shall, however, be mandatorily payable (except as otherwise provided by the last sentence in this paragraph) only out of Available Net Income of the New Company in respect of such Income Periods or (in the case of accumulations of interest) out of Available Net Income in respect of such Income Periods or subsequent Income Periods; the Board of Directors of the New Company may, however, in its discretion, cause the payment of interest on the new Income Mortgage Bonds out of any funds whatever that may be lawfully available therefor. Interest on the outstanding Income Bonds (excluding Bonds held in the sinking fund) shall be paid if covered by Available Net Income, and, if not fully covered thereby, then to the extent so covered, in multiples of ¼%; any Available Net Income remaining undistributed shall to the extent of the interest for such Income Period on the Income Bonds that accrued but was not paid be held in the treasury of the [fol. 481] New Company and added to the Available Net Income for the next succeeding Income Period. Interest on the new Income Bonds shall be cumulative to a maximum amount due any one time of 22½% of their principal amount

(whether such amount represents interest for consecutive or non-consecutive Income Periods). Accumulations of interest shall not bear interest. In case of accumulations of interest, the earliest due coupons or instalments of interest shall be paid first. When the principal of any of the new Income Bonds shall become payable, whether at maturity or upon redemption or by acceleration or in any other manner, or a permanent or confirmed appointment shall be made of any Trustee or Receiver for the New Company or its property, all accumulated interest on such bond or bonds shall become immediately and absolutely payable regardless of earnings.

The holders of the Income Bonds which are fully registered or registered as to principal shall have one vote per $1,000 principal amount of such bonds in the election of one member of the Board of Directors of the New Company, such right to be exercised by a majority of such bonds present or represented at any meeting to the exclusion of all other security holders. In the discretion of the Reorganization Committee the new Income Mortgage may make suitable provision for extending such voting right to include holders of bonds payable to bearer, and for the exercise thereof.

The Income Bonds shall be redeemable in whole or in [fol. 482] part, on any interest payment date, on thirty days' notice by publication, at their principal amount plus interest at the rate of 4½% per annum accrued since the next preceding 1st day of April or October, whichever is the nearer, plus any unpaid accumulated interest.

The Income Bonds will be entitled to the benefit of a sinking fund to be created by the payment on April 1st and October 1st of each year of an amount equal to one-eighth of 1% of the aggregate principal amount of such bonds to be issued in the reorganization. Such semi-annual payments shall be payable only out of Available Net Income after payment, or setting aside for payment, of all accumulations of interest and of the full interest requirements at the rate of 4½% per annum for the applicable Income Period on the Income Bonds outstanding. Such semi-annual payments for the sinking fund shall be cumulative to a maximum number at any one time of ten instalments (whether consecutive or non-consecutive instalments). Moneys in the sinking fund shall be applied to the retire-

ment of Income Bonds by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders and, to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. The bonds so purchased or redeemed shall be held alive in the sinking fund and shall continue to bear interest for the purposes of the sinking fund, and interest payable thereon (calculated at the rate paid for the ap- [fol. 483] plicable Income Period, including accumulations, on outstanding Income Bonds) shall be added to the instalments of sinking fund above provided for. No Income Mortgage bonds shall be issued in lieu of the Income Bonds so purchased or redeemed for the sinking fund.

The new Income Mortgage shall contain a covenant by the New Company that it will not create any mortgage or other lien securing debt issued by it other than the new First Mortgage and the new Income Mortgage on any of the properties or systems acquired by it under the Plan.

The new Income Mortgage shall provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof and of any or all supplements thereto and of the rights and obligations of the New Company thereunder and of the holders of the bonds at any time by the concurrent action of the New Company and of the holders of not less than two-thirds in aggregate principal amount of the bonds then outstanding; and such modification or alteration may specifically include procedural provision for ascertaining Available Net Income without the maintenance of separate books of account in the event that the New Company shall be merged or consolidated or unified with a new company to result from the reorganization of The Western Pacific Railroad Company or with any other corporation; provided, however, that no such change or modification shall (a) alter or impair [fol. 484] the obligation of the New Company to pay the principal of or accumulated interest on any bond, or to pay interest on any bond out of available Net Income as determined by the provisions hereof or by any such alteration or modification of such provisions, at the time and place and at the rate and in the currency provided in such bond without the consent of the holder of such bond, or (b) permit the creation by the New Company of any mortgage or lien in the nature of a mortgage ranking prior to or

ments on such Notes (including accumulations of interest) shall be applied to the payment of the principal amount of such Notes. Such Notes may be redeemed in whole or in part at any time on thirty days' notice at their principal amount plus full interest at the rate of 4% per annum accrued since the last preceding October 1st or April 1st, whichever is the nearer, and all unpaid accumulated interest. Upon the payment or other retirement of all such Notes, the collateral securing them shall be returned to the New Company, and the New Company shall, in the case of certificates of stock, cancel and retire the same, and in the case of bonds deliver the same forthwith to the Trustee under the indenture securing the same for cancellation and retirement; no bonds shall be issued in lieu of any bonds so cancelled and retired.

[fol. 494] *Preferred Stock*

The charter of the New Company will initially authorize 315,000 shares of new Preferred Stock, of which 314,350 shares of the par value of $100 each are to be issued in the reorganization as set out in Article V below.

Such new Preferred Stock shall be known as Series A and shall be entitled to receive dividends out of Available Net Income as hereinabove provided or out of earned surplus from prior Income Periods, when and as declared by the Board of Directors of the New Company, at the rate of 5% per annum in respect of each calendar year beginning January 1, 1937, before any dividends shall be paid or declared or set apart for payment on the Common Stock. Such dividends shall be cumulative to the extent earned in respect of any Income Period but not paid; for the purpose of the foregoing provision dividends shall be deemed to have been earned in any Income Period to the extent covered by Available Net Income in such Income Period plus payments into the Capital Fund in respect of such Income Period; but such dividends shall otherwise be non-cumulative. In any liquidation or winding up or distribution of the assets of the New Company, whether voluntary or involuntary, the new Preferred Stock of Series A shall be entitled to receive out of the assets of the New Company its par value plus any accrued and unpaid cumulative dividends thereon, before any distribution shall be made to any Common Stock, but shall not be entitled to any further participation in any

[fol. 495] such assets. The new Preferred Stock of Series A shall be redeemable in whole or in part at any time at its par value plus accumulated and unpaid dividends and proportionate dividend for the current year. Holders of the new Preferred Stock of Series A shall be entitled to one vote per share for the election of two members of the Board of Directors of the New Company, such right to be exercised by a majority of such stock present or represented at any meeting to the exclusion of all other security holders.

The new Preferred Stock of Series A shall be convertible at the option of the holder at any time on or before fifteen days prior to the date as of which such stock shall have been called for redemption, into new Common Stock of Class A, at the rate of one share of new Common Stock of Class A for each share of new Preferred Stock of Series A. If as a result of such conversions or of redemption or in any other way, the aggregate par value of the new Preferred Stock of Series A at any one time outstanding shall be reduced to $10,000,000 or less, then the holders of new Preferred Stock of Series A shall cease to be entitled to elect two members of the Board of Directors of the New Company and such Directors shall be elected by the holders of the Common Stock of Class A in addition to the Directors elsewhere herein provided for election by the holders of new Common Stock of Class A.

The New Company shall not, without the vote or consent of the holders of at least two-thirds in par value of the outstanding new Preferred Stock of Series A and in number of [fol. 496] shares of the outstanding new Common Stock of Class A, voting as separate classes, (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new First Mortgage and new Income Mortgage hereinbefore mentioned and purchase money liens (including equipment trust liens) upon property hereafter acquired given for not more than 75% of the purchase price of such property; (2) create or issue or assume any bonds, notes or other evidences of indebtedness maturing more than two years from their date, other than those to be authenticated and delivered or assumed under the Plan, except purchase money obligations given or existing obligations assumed for not more than 75% of the purchase price of property acquired by it; (3) purchase or acquire or contract to purchase or acquire any property or system of properties

at a cost to the New Company of $5,000,000 or more in cash or principal amount or par or book value of securities; (4) enter into any lease or trackage contract calling for an annual rental to be paid by the New Company of $200,000 or more; (5) make any loans in an aggregate amount exceeding at any one time the aggregate amount of $200,000 to any subsidiary or parent or affiliated or other interest except by way of purchase of bonds of such borrower and pledge thereof under the new First Mortgage subject to the conditions and restrictions to be provided therein; (6) create any class of, or issue any, stock ranking either as to assets or as to dividends, in priority to or on a parity with, the new [fol. 497] Preferred Stock of Series A; (7) merge or consolidate with any other corporation or dispose by sale or lease or otherwise of its assets as an entirety or substantially as an entirety; or (8) make any amendment to its charter or certificate of incorporation affecting the rights or interests of such stockholders. No additional shares of Preferred Stock other than those to be issued under the Plan ranking prior to the Common Stock of Class A, and no additional shares of Common Stock of any class other than those to be issued under the Plan, shall be issued without the vote or consent of the holders of at least two-thirds in number of shares of the Common Stock of Class A then outstanding. In the event that the New Company shall be merged or consolidated or unified with a new company to result from the reorganization of The Western Pacific Railroad Company, or with any other corporation, then by vote or consent of two-thirds in par value of the Preferred Stock of Series A then outstanding procedural provision may be made for ascertaining Available Net Income without the maintenance of separate books of account, and such provision shall be binding on all the holders of stock of such Class.

New Common Stock

The charter of the New Company will initially authorize (1) 513,458 shares of new Common Stock of Class A, of no par value, all of which will be issued, or reserved for issuance upon the exercise of Warrants, in the reorganization, [fol. 498] plus (2) such number of shares as shall be necessary to provide for (a) the conversion privilege of the new Preferred Stock of Series A and (b) the treatment herein-

after stated for general creditors, all of which shall be reserved therefor.

The charter of the New Company will initially authorize 400,000 shares of Common Stock of Class B, of no par value, all of which will be reserved for issuance upon the exercise of the Warrants and Option to be issued in the reorganization.

The shares of Common Stock of Class A and Common Stock of Class B shall be identical in all particulars except: (1) on any liquidation or winding up or distribution of the assets of the New Company, whether voluntary or involuntary, the new Common Stock of Class A shall be entitled to receive out of the assets of the New Company the sum of $100 per share plus any dividends declared and unpaid before any distribution shall be made to the Common Stock of Class B, and after each share of the Common Stock of Class B shall have received an equal amount, any remaining amount shall be divided among the holders of Common Stock of Classes A and B equally share for share; (2) the voting rights of the two classes shall be as follows: the holders of shares of new Common Stock of Class A shall, in addition to the voting rights above provided, be entitled to one vote per share for the election of two members of the Board of Directors of the New Company, such right to be exercised by a majority of such stock present [fol. 499] or represented at any meeting to the exclusion of all other security holders; the holders of shares of new Common Stock of Class B shall be entitled to one vote per share on all matters except to the extent that provision is herein made for election of Directors by other classes of securities; provided, however, that unless and until 200,000 or more shares of new Common Stock of Class B shall be outstanding the holders of shares of new Common Stock of Class A shall be entitled to one vote per share on all matters except to the extent that provision is herein made for election of Directors by holders of new Income Mortgage Bonds or new Preferred Stock of Series A. In voting for Directors the holders of shares of Common Stock of Class B shall be entitled to cumulative voting rights to the extent permitted by law.

Any vote or consent by the holders of Preferred Stock of Series A or Common Stock of Class A authorizing the issuance of additional shares of stock of any kind or of securities convertible into the same may waive on such

terms and conditions, if any, as may be specified in such vote or consent, the preemptive right of all the holders of shares of stock of such Series or Class, as the case may be, to subscribe to such additional shares or securities.

All shares of Common Stock whether of Class A or of Class B, issued under the Plan, shall be issued to the Reorganization Committee as Voting Trustees, to be held by them for a period of three years from the creation of such Voting Trust subject to the following provisos: (1) the Voting [fol. 500] Trustees may at any time terminate such Voting Trust; and (2) if and when the Option hereinbelow provided for shall be exercised and the price for the stock called for thereby paid to the New Company, the Voting Trust shall be terminated within ninety days after the date of such payment. The reasonable expenses of the Voting Trustees, including counsel fees, shall be paid by the New Company.

Board of Directors

The Board of Directors of the New Company shall consist of 12 members. One member shall be elected by the holders of Income Mortgage Bonds as aforesaid, two by the holders of Preferred Stock of Series A and two by the holders of Common Stock of Class A. The remaining members shall be elected by the holders of Common Stock of Class B, and one of such remaining members shall be the president of the corporation. If no Director or Directors shall be elected by the holders of new Income Mortgage Bonds or Preferred Stock of Series A or Common Stock of Class A for any year, such Director or Directors may be elected for such year by the holders of Common Stock of Class B.

Warrants and Option

There will be issued 164,456 Warrants of Series A, each giving the holder thereof the right to purchase a Voting Trust Certificate (or after termination of the voting trust, a [fol. 501] certificate) for one share of new Common Stock of Class A at the price of $20 per share at any time within three years from the date of effectuation of the Plan, and at $30 per share within the next following three years.

There will also be issued two Warrants of Series B, each giving the holder thereof the right to purchase a Voting Trust Certificate (or after termination of the voting trust, a certificate) for 100,000 shares of new Common

Stock of Class B at the price of $30 per share at any time within three years from the date of effectuation of the Plan, and at $45 per share within the next following three years.

There shall be issued to the Reorganization Committee an assignable option (which may be exercised by one or more persons severally, in whole or in part) or options (herein sometimes called the Option) to buy at any time within three years from the date of effectuation of the Plan 200,000 shares of the new Common Stock of Class B at such price or prices (not less than $30.00 per share) as may then be fixed by the Reorganization Committee and approved by the Interstate Commerce Commission. The Reorganization Committee shall be authorized to transfer or assign such Option to any interests whom they may select as being to the greatest advantage of the New Company and its earning power, in consideration of an agreement by such transferee or transferees or assignee or assignees with the Reorganization Committee and the New Company to exercise such Option and to make payment to the New Company at a time and price to be then fixed [fol. 502] subject to the approval of the Commission; in any case, however, such transfer or assignment shall be made only to such transferee or transferees or assignee or assignees and at such price and upon such other terms and conditions as may be approved by the Commission.

Any cash proceeds received by the New Company from the exercise of the Warrants of Series A and Series B and from the exercise of the Option shall be used to redeem the new Income Mortgage Bonds then outstanding issued under the Plan to RFC; any balance then remaining shall be used to redeem an amount of new First Mortgage Bonds equal to (and of the same series as) the amount thereof that shall have been issued under the Plan upon conversion of said Income Bonds issued to RFC or to provide funds to redeem or pay certificates of indebtedness issued by the Trustees of the Denver or the Trustee of the Salt Lake Western and to provide funds for the payment of reorganization expenses and working capital and any balance then remaining shall be paid as an additional contribution to the Income Mortgage Sinking Fund.

V

Treatment of Existing Securities

The new securities above designated are to be distributed among the holders of outstanding senior bonds on the following bases for each $1,000 principal amount of bonds:

[fol. 503]

	First Mortgage Bonds	Income Bonds	Preferred Stock	Total
Junction Bonds	$1,079.10			$1,079.10
First Trust 4's	1,080.00			1,080.00
Eastern Consol. 4's	476.70	$272.80	$350.50	1,100.00
Eastern Consol. 4½'s	482.10	275.90	354.40	1,112.40
Western Consol.	511.00	579.00		1,090.00
R & I 5's	70.80	174.00	867.60	1,112.40
R & I 6's	72.20	177.50	885.10	1,134.80

The amounts of new First Mortgage Bonds distributed to the Junction Bonds and the First Trust 4's equal the principal amount of such bonds plus unpaid interest accrued thereon to January 1, 1937. In addition the Junction Bonds will receive $29.17 in cash per $1,000 principal amount to compensate for the reduction in their coupon rate to their maturity on December 1, 1939.

The amounts of new First Mortgage Bonds and Income Bonds distributable to the other bonds above listed are proportionate to the relative rights, earning power and fair value of such bonds as determined by the Committee. In making such determination the Committee, without prejudice to the assertion by it of any greater claims in the event of opposition to the Plan, but expressly reserving the right to assert such claims, has endeavoured to avoid litigation with respect to liens on equipment by not presently claiming a lien on substantial parts thereof as against the R & I Bonds. Further to promote such policy of a just and equitable plan which may avoid the expense and delay of litigation by winning acceptance from all interests, the Committee, without prejudice to the assertion by it of any different claims in the event of opposition to the Plan, but [fol. 504] expressly reserving the right to assert any such claims, has assigned to the R & I Bonds the substantial surplus of new Income Bonds issuable in respect of the collateral pledged with RFC.

In the allocations to all bonds listed in the above table interest accrued to January 1, 1937, and unpaid has been

added to principal and their sum treated as one integral debt. The par amounts of Preferred Stock distributable to such bonds equal the remainder of such principal and interest not provided for in senior securities.

The General Mortgage Bonds will receive 11.7 shares of Common Stock of Class A for each $1,000 principal amount of such bonds, being at the rate of $100 per share for the principal amount plus all unpaid interest accrued thereon to January 1, 1937, except the contingent interest accrued in the five-year period ended February 1, 1929.

RFC will be asked to underwrite the refunding of the Salt Lake bonds through the sale of new First Mortgage Bonds of Series B or some other series other than Series A at such price as may be determined by the Reorganization Committee or the New Company subject to the approval of the Commission. In consequence it is assigned the earnings on the Salt Lake stock as increased by the savings from such refunding. The earnings assigned to the Dotsero Cut-Off include an allowance designed to make adequate provision for the special factors in its situation. RFC is further assigned the securities issuable in respect of its other [fol. 505] pledged securities. On that basis it will receive 61% of the principal amount of its debt in new First Mortgage Bonds Series B and the residue of its principal and all unpaid interest accrued to January 1, 1937, in new Income Mortgage Bonds. As hereinabove provided, proceeds received from the exercise of the Warrants and the Option shall be used first to redeem the new Income Mortgage Bonds to be issued to RFC. Appropriate provision shall be made that each of the new Income Mortgage Bonds so issued to RFC shall, unless called for redemption and payment duly provided within the period of three years after the date of its issuance, be convertible, on the next following first day of April or first day of October (whichever is the closer to the expiration of said period), after not less than fifteen days prior notice, when surrendered with all unpaid appurtenant coupons, into new First Mortgage Bonds of Series B having (subject to the provision hereinbelow with respect to the issuance of scrip for fractional parts of bonds) a principal amount equal to the sum of the principal of the Income Bonds so surrendered plus interest at the rate of 4% per annum on the principal of such Income Bonds from the date of issuance thereof less all amounts

paid by way of interest on such Income Bonds on or before such conversion date. All Income Bonds surrendered on conversion shall be cancelled, and no Income Bonds shall be issued in lieu thereof. In view of the foregoing provisions, the surplus of the securities issuable in respect of [fol. 506] the collateral pledged with RFC (including second liens on other collateral) has not been assigned to it. The Income Bonds of the Salt Lake now pledged with RFC and any Salt Lake bonds held in the treasury of the Salt Lake are to be cancelled in the reorganization.

The debt to RFC remaining at the time after application of all distributions to the Denver under the Marshaling and Distributing Plan will be paid at the election of the New Company and/or the Reorganization Committee, either (1) in cash within thirty days after the date of effectuation of the Plan in full of principal and interest at 1½% to such date of effectuation, or (2) by a promissory note in the principal amount of such cash payment, payable on or before six months from such date of effectuation, bearing interest at 4% and secured by the securities issuable in respect of the bonds pledged for the existing debt. Upon the payment of such note, the collateral securing the same shall be returned to the New Company, and the New Company shall, in the case of certificates of stock, cancel and retire the same, and in the case of bonds, deliver the same forthwith to the Trustee under the indenture securing the same, for cancellation and retirement. No bonds shall be issued in lieu of any bonds so cancelled and retired.

The Chase Bank will receive Contingent Ten Year Collateral Notes as described above, under which there will be [fol. 507] pledged the securities issuable in respect of the bonds pledged to secure the existing debt.

Holders of claims against the Denver or the Salt Lake Western not having any lien and not entitled to priority of payment over any mortgage bonds, including claims for damages arising from the disaffirmance of leases or other executory contracts, whether of the Denver or of its Trustees or of the Salt Lake Western or of its Trustee, shall receive new Common Stock of Class A, on the basis of $110.00 per share, for the amount allowed by the Court on their claims, including, to the extent so allowed, interest to January 1, 1937.

Holders of Preferred Stock will receive per share one Warrant of Series A, above described, and each of the two

holders of Common Stock will receive one Warrant of Series B, above described.

Holders of the 460 shares of stock of the Salt Lake which are still outstanding in the hands of the public will receive the securities stated in the following table or in the event of their failure or refusal to accept such offer they will eventually be given such consideration, if any, as they may otherwise become entitled to receive under the law as a result of the unification.

The $2,175,000 principal amount of Equipment Trust Certificates issued by the Trustees of the Denver since January 1, 1937, and any other Equipment Trust Certificates that may hereafter be issued by them will, to the extent that [fols. 508-509] the same remain outstanding at the time the New Company comes into possession and ownership of the properties of the Denver, be assumed by the New Company in pursuance of the decrees authorizing the issuance of such certificates. Any certificates of indebtedness issued by the Trustees of the Denver or the Trustee of the Salt Lake Western and outstanding at the time of reorganization are to be redeemed or paid from the proceeds of new First Mortgage Bonds reserved for that purpose as hereinabove provided.

If interest shall be paid on any bonds or other obligations of the Denver or Salt Lake Western prior to the date when the New Company comes into possession and ownership of their properties, the amount so paid will be deducted, in the case of all outstanding bonds or obligations other than the Junction Bonds, from the amount of their total claim used as a basis for the distribution of new securities, and, in the case of the Junction Bonds, first from the amount of cash payable to the Junction Bonds as an adjustment of interest rates as aforesaid, and then from the total amount of their remaining claim.

The treatment proposed for the various securities is shown in detail in the following table:

(Here follows 1 paster, folio 510)

[fol. 510]

DISTRIBUTION OF NEW SECURITIES

Present Liabilities as of January 1, 1937	Principal Amount[1]	Accrued Interest	Undisturbed	New First Mortgage Bonds	Per Cent of Principal	New Income Bonds	Per Cent of Principal	New Preferred Stock	Per Cent of Principal	New Common Stock, Class A (Shares)	Warrants[8]
D&RGW:											
Equipment Trusts[2]	$1,805,000		$1,805,000								
Junction Bonds	2,000,000	$158,333		$2,158,333	107.91						
First Trust 4's	15,190,000	1,215,200		16,405,200[4]	108.00						
Eastern Consol 4's	34,125,000	3,412,500		16,267,780[5]	47.67	$9,310,3	27.28	$11,959,335	35.05		
Eastern Consol 4½'s	6,382,000	717,975		3,076,945[5]	48.21	1,760,9	27.59	2,262,031	35.44		
Western Consols	15,080,000	1,357,200		7,706,697[5]	51.10	8,730,503	57.90				
R&I 5's	12,000,000	1,350,000		850,230[5]	7.08	2,088,118	17.40	10,411,652	86.76		
R&I 6's	2,000,000	270,000		144,571[5]	7.22	355,058	17.75	1,770,371	88.51		
RFC	10,691,850	626,108		6,530,057[6]	61.07	4,787,901	44.78				
Chase Bank[6]	1,500,000	93,948		419,887[6]	27.39	1,009,116	67.27	5,031,597	335.44		
General Mortgage Bonds	29,808,000	5,092,200[3]								349,002	
Preferred Stock (par value)	16,445,000										164,456[9]
Common Stock (shares)	300,000										200,000[9]
D&SL:											
First Mortgage Bonds	1,500,000			11,443,675[11]							
Income 6's[12]	9,734,000										
Stock with Public (shares)	460			37,242		9,931					
Total	$14,293,464	$1,805,000		$65,031,617[10]		$28,052,011		$31,434,986		349,002	364,456[7]
Annual Fixed Charges		$89,408		$2,601,265[10]							
Annual Contingent Interest						$1,262,340					
Annual Preferred Dividend								$1,571,749			

NOTES:

[1] Excluding pledged bonds.

[2] Since January 1, 1937, the Trustees of the Denver have issued $2,175,000 principal amount of Equipment Trust Certificates, which will also be assumed by the New Company.

[3] Excluding the $7,452,000 of contingent interest accrued in the five year period ended February 1, 1929.

[4] Series A; interest computed at 4%, but may be increased to not exceeding 4½% as provided in the Plan. In addition the Junction Bonds received $58,333 because of reduction in coupon rate by 1% to their maturity.

[5] Series B.

[6] Securities issuable to the Chase Bank are to be pledged as collateral for the new Contingent Ten Year Collateral Notes.

[7] In addition an option for 200,000 shares of Common Stock of Class B is to be issued to the Reorganization Committee as and for the purposes herein provided.

[8] Series A.

[9] Series B. And see Note (7).

[10] Excludes provision for $6,000,000 principal amount of new First Mortgage Bonds reserved to be issued if and to the extent necessary to retire Trustee's Certificates, pay reorganization expenses and provide working capital. The amount of Series B Bonds may possibly be increased through conversion of the new Income Mortgage Bonds to be issued to RFC, as provided in the Plan. And see Note (4).

[11] Includes bonds to be issued to provide for the redemption premium of 1% on the Salt Lake First Mortgage Bonds and 2% on the Salt Lake Income 6's.

[12] Excludes $1,266,000 principal amount pledged with RFC, to be cancelled under the Plan.

GENERAL NOTE: The debt to RCC ($297,409 as of January 1, 1937) less subsequent distributions will, as provided in the Plan, be paid either in cash or in a six months note secured by the following collateral: $300,283 principal amount of new First Mortgage Bonds Series B, $171,858 principal amount of new Income Mortgage Bonds and $220,752 par value of new Preferred Stock of Series A. If such note is issued, upon payment thereof the collateral will be retired and cancelled. In view of such fact and the short maturity, neither the note nor the collateral is included in the above table.

[fol. 511] VI

Claims Not Affected by the Plan

The following claims are not affected by the Plan:

(a) Liabilities of the Salt Lake other than its bonds and capital stock pledged with RFC;

(b) Current liabilities of the Denver incurred in the ordinary conduct of business prior to the institution of the proceedings under Section 77 of the Bankruptcy Act, which are entitled to priority over any mortgage bonds of the Denver.

(c) Current liabilities and obligations of the Denver and the Salt Lake Western and of the Trustee(s) thereof incurred during said proceedings; and

(d) All other claims, liabilities and obligations for which no specific provision is made in the Plan.

To the extent that such claims, liabilities and obligations shall not have been paid by the Denver or the Salt Lake Western or the Trustee(s) thereof, they are to be paid in cash or assumed by the New Company. All such claims, liabilities and obligations may be adjusted or compromised and dealt with, paid or discharged by the New Company, in such manner and to such extent as may be determined by the Board of Directors of the New Company subject to the approval of the Court.

The New Company shall have the right to take such action with respect to the lease or agreement with The Northwestern Terminal Railroad Company as may be lawful under the terms thereof and may adjust, compromise, [fol. 512] deal with, pay or discharge any claim on or arising from such agreement to the extent and in the manner that may be approved by the Board of Directors of the New Company subject to the approval of the Court. Except for such agreement with The Northwestern Terminal Railroad Company and except for agreements, leases and trackage contracts between the several companies embraced within the Plan, the New Company shall be deemed to have assumed all such contracts of the Denver, the Salt Lake and the Salt Lake Western which are executory in whole or in part, including any executory leases; joint facility agree-

ments and guaranties as shall not have been disaffirmed by the Denver or the Salt Lake Western or the Trustee(s) thereof acting with the approval of the Court in said proceeding prior to the date of confirmation of the Plan, and also, with the above exceptions, any executory contracts, including any executory leases, joint facility agreements and guaranties made by the Denver or the Salt Lake Western or the Trustee(s) thereof, with the approval of the Court in said proceedings, which, by their terms, do not terminate at the conclusion of said proceedings.

VII

Provisions for Effectuation of the Plan

No holder of any security of any of the companies embraced within the Plan which is affected thereby shall be requested to accept the Plan until after a public hearing [*513] thereon shall have been held under Section 77 of the Bankruptcy Act as the same now exists or may hereafter be amended, and a report and order of the Commission approving the Plan (in its present form or as it may be modified as hereinafter provided) and finding that the Plan complies with said Section 77, or until the Court in said proceedings shall have taken such action as may be required by said Section 77 prior to the submission of a Plan thereunder to security holders or creditors, and thereafter the Plan shall be submitted to the security holders and creditors of the Denver and the Salt Lake Western in accordance with the provisions of said Section 77.

The Plan shall not be carried out until it shall have been accepted by or on behalf of the holders of at least two-thirds in principal amount of each class of the outstanding bonds of the Denver, as such bonds have been or may hereafter be classified for the purpose of the Plan by the Court in said proceedings, and by RFC, nor unless either (1) the Plan shall have been accepted by or on behalf of creditors (other than bondholders and RFC) of each class affected by the Plan as the same have been or may be classified by the Court in said proceedings, holding at least two-thirds in principal amount of the total allowed claims of such class, and by or on behalf of the stockholders of each class holding at least two-thirds of the stock of such class, or (2) provision shall have been made for protecting the interests of such nonassenting classes of creditors and stockholders as herein-

[fol. 514] after in Article VIII provided; the foregoing requirement for consent is subject, however, to the provision that the Reorganization Committee may in its discretion, subject to any requirements of the applicable law, at any time prior to the entry of a final order by the Court confirming the Plan or refusing to confirm the same, eliminate said requirement for consent as to any class of bondholders or RFC upon substituting therefor the provision for protecting the interests of such non-assenting class or classes as hereinafter in Article VIII provided.

The Committee's acceptance and proposal of the Plan are dependent upon, and limited to, the provisions stated herein as an entirety, all of such provisions being interdependent; no provision in the Plan shall be deemed an admission, relinquishment, disclaimer or waiver of any legal or equitable rights of any class of bonds as against any other class of bonds or other debt or stock. If any change of any kind in any of said provisions shall be required by the Commission or the Court or otherwise, then (1) the Committee and each member thereof reserve the right to assert any further claims without limitation, whether or not stated herein, whether the same as or different from any statement herein, and whether consistent or inconsistent with any statement herein; and (2) neither the Committee nor any member thereof shall have any further obligation or responsibility in the premises unless and until the Committee shall have accepted such change by modifying the Plan in accordance [fol. 515] therewith as herein provided. No member of the Committee who shall not have accepted or approved any such modification shall be bound by such action of the Committee.

Upon confirmation of the Plan, it shall be carried out under the supervision of a Reorganization Committee to consist of the following members: four members to be designated by Insurance Group Commitee as representatives respectively for the First Trust 4's, the Junction Bonds, the Eastern Consols and the Western Consols; one member to be designated by the Trustee under the Indenture securing the R&I Bonds as the representative for such bonds; one member to be designated by the Trustee under the Indenture securing the General Mortgage Bonds as the representative for such bonds; and one member to be designated by RFC as its representative. If no representative

shall be so designated by the three interests last aforesaid, within such period as the residue of the Reorganization Committee may determine after confirmation of the Plan, the foregoing provision for such representatives shall cease to be effective.

The Plan may be carried out either by revesting the properties of the Denver or its Trustees and the Salt Lake Western or its Trustee in either or both of said companies of by transferring said properties to some other existing corporation or to a new corporation organized for the purpose, and the execution by the corporation in which said properties shall be vested of the new mortgages and the [fol. 516] issuance by it of the new securities contemplated by the Plan. The corporation so acquiring said properties and issuing the new securities is (together with its successors and assigns) herein referred to as the New Company. The date of effectuation of the Plan as such phrase is, or other words of like import are, used herein shall mean the date on which such company shall come into possession of said properties. The Plan may be carried out with respect to the Salt Lake by either merger or consolidation or sale of assets, or in any other manner that the Reorganization Committee may determine, in all cases subject to the approval of the Commission as and to the extent provided by law.

Scrip may be issued and distributed in lieu of fractions of a share of stock or fractional parts of bonds. Holders of scrip for fractions of a share of any new stock will not be entitled to receive dividends or vote or exercise any other rights of stockholders in respect thereof. Scrip for fractional parts of bonds may be made non-interest bearing and shall be non-voting. The New Company shall, however, make appropriate provision for combining such fractions of shares of stock into whole shares and such fractional parts of bonds into whole bonds. The Reorganization Committee may make such adjustments in the allowance of interest accrued on outstanding securities as may be necessary to avoid the issuance of scrip in fractional amounts which they may deem too small for practical purposes.

The method and procedure for effectuating the Plan shall [fol. 517] be determined by the Reorganization Committee in its discretion, and the Reorganization Committee shall also determine the form, and, to the extent not inconsistent herewith, the provisions, of all mortgages, bonds, coupons,

charters, by-laws, stock certificates, voting trust certificates, purchase warrants, subscription warrants, options, acceptances, assents, certificates and all other instruments which may in the judgment of the Reorganization Committee be either necessary or desirable in connection with the effectuation of the Plan, subject, to the extent now or at the time provided by law, to the approval of the Court and/or Commission or other tribunal having jurisdiction in the premises. The Reorganization Committee or the New Company may make such arrangements for underwriting the issue and exchange or sale of the new First Mortgage Bonds to be issued to refund said Trustees' Certificates and bonded debt of the Salt Lake and pay reorganization expenses and provide working capital as they or it may deem appropriate in their or its discretion subject to the approval of the Commission and the Court in said proceedings.

The Reorganization Committee may from time to time add to its members; it may act by a majority of its members at from time to time constituted, at a meeting or in writing without a meeting. The Reorganization Committee may employ such agents, attorneys and others as it may deem desirable for the purposes of the Plan. The Reorganization Committee may from time to time delegate to others [fol. 517a] any power or discretion conferred upon it by the Plan; Any member of the Reorganization Committee may resign at any time by filing a written resignation with the Commission; the Reorganization Committee may fill any vacancies created by death, resignation or otherwise, preserving the representation on said Committee of the several interests as hereinbefore provided. The members of the Reorganization Committee shall not be liable for any action taken or failed to be taken by them in good faith, or by any person employed by the Reorganization Committee in good faith, or otherwise, except for their respective individual wilful default. The members of the Reorganization Committee shall agree to serve without compensation, but its expenses shall be reimbursed as hereinafter provided.

The Reorganization Committee may from time to time, whether before or after the acceptance of the Plan by any holders of securities or creditors, supplement or modify the Plan or adopt a substitute Plan, subject to the provisions of said Section 77, or may entirely abandon the Plan

or any modified or substitute Plan, by filing a written notice to that effect with the Commission. The term Plan as used herein shall be deemed to include any such supplemented, modified or substitute Plan.

Unless otherwise provided in said Section 77 or any order or orders of the Court in said proceeding or of the Commission, whenever notice shall be required or permitted to be given under or pursuant to the Plan, such notice shall [fol. 517b] be given by publishing a copy of such notice once in each week on any secular day of such week for two consecutive weeks in one newspaper published and of general circulation in the Borough of Manhattan, City and State of New York, and in one newspaper published and of general circulation in the City of Denver, Colorado. In addition the Reorganization Committee shall (1) in case of notices to security holders who have accepted the Plan, mail such notices, postage prepaid, to the addresses of such security holders as set forth in the acceptances signed and filed by them, and (2) in case of notices to security holders who shall not have accepted the Plan, by mailing such notices, postage prepaid, to such security holders whoses names and addresses appear in the record before the Court in said proceedings or on the books of the companies embraced within the Plan or of the New Company, as the case may be, but failure to mail any such notices, or delay in mailing any such notices, shall not invalidate the notice by publication above provided for, which alone shall be sufficient.

All expenses in connection with the Plan and its effectuation, and all costs of administration and other allowances made by the Court in said proceeding shall be paid by the New Company, subject to the provisions of said Section 77, and shall constitute a charge upon the properties of the New Company as a cost of administration prior in lien to all new securities issued under the Plan.

There shall be included in such expenses such reasonable [fol. 518] compensation for necessary services rendered and reimbursement for actual expenses incurred in connection with said proceeding and the development and effectuation of a plan (whether in connection with the negotiation of the plan heretofore proposed by the Denver in said proceedings or in connection with this Plan or in connection with any other plan that may hereafter be proposed) by the Trustees under said mortgages, the Committee or

representatives of certain of its members prior to its formal organization, the Reorganization Committee and all other parties in interest (including other representatives of creditors and security holders of the Denver, the Salt Lake Western and the Junction) and the attorneys or agents of any thereof (including the Denver, the Salt Lake Western and the Junction) as may be approved or allowed by the Commission and the Court in said proceeding.

VIII

Provision for Dissenting Creditors and Stockholders

If the holders of more than one-third in principal amount of any class of creditors (other than holders of bonds or RFC, except to the extent that the above requirement for a two-thirds consent by the holders of any such class of bonds or RFC may have been eliminated by the Reorganization Committee as above provided) of the Denver, the Salt Lake Western and the Junction, as they have been or may be classified by the court in said proceeding, or the holders of more than one-third of the shares of stock of any class of [fols. 519-521] the Denver shall not have accepted the Plan within such period as the Reorganization Committee, with the approval of the Commission and the Court, may determine, after holders of at least two-thirds in principal amount of each class of bonds affected by the Plan and on the part of which two-thirds consent shall be required by the Plan as now existing or hereafter modified, shall have accepted the Plan, the property of the Denver shall be sold at public auction at not less than a fair upset price as determined by the Court in said proceeding, and the non-assenting creditors of such class and/or the non-assenting stockholders of such class shall be entitled to receive their aliquot proportion of the proceeds of such sale, after deducting therefrom all expenses of such sale and the amount which would be required to pay in full, of principal and unpaid interest accrued to the date of such sale, all creditors whose claims are prior in lien or superior in equity to the claims of such non-assenting creditors or the rights of such non-assenting stockholders. Upon any such sale the property may be purchased for the benefit of the New Company in the reorganization by the Reorganization Committee, and in that event there shall be applied on account of the pur-

chase price therefor the distributive share of the proceeds of sale of all securities the holders of which shall have assented to the Plan and the securities, though not assenting to the Plan, of all classes of which two-thirds or more in amount have assented to the Plan.

Dated as of January 1, 1937.

Filed June 15, 1937, 2:00 P. M. Charles W. Bishop, Clerk.

[fol. 522] INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION [1]

Submitted Decided

Plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act as amended, recommended.[2]

F. C. Nicodemus, Jr., and *William V. Hodges* for Denver & Rio Grande Western Railroad Company, Denver & Salt Lake Western Railroad Company and Rio Grande Junction Railway Company.

Henry W. Anderson, George D. Gibson, Leighton H. Schurbeck, Oscar R. Ewing, Harry Hoffman, Edgar J. Goodrich, Mildred E. Reeves, John B. Marsh, Edward E. Watts, Jr., Fred N. Oliver, Karl Michelet, Charles J. Nas-

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[1] This report also embraces reorganization and consolidation of the Denver & Salt Lake Western Railroad Company, secondary debtor, and the Denver & Salt Lake Railway Company, the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company, none of the last three having filed petitions under section 77.

[2] Previous reports: 212 I. C. C. 105 and 709; 217 I. C. C. 101; 224 I. C. C. 574. Orders entered without report (other than orders permitting interventions) January 21, August 8, and September 4, 1936; January 9, April 12, May 26, and October 27, 1937.

myth, John E. Benton, Clyde S. Bailey, Simon Fleishman, Clarence R. Freeman, Stanley Marsh, Robert McKinney, W. Heyward Myers, Jr., Philip B. Fisher, William Clarke [fol. 523] *Mason, Edwin S. S. Sunderland, Thomas O'G. FitzGibbon, Malcolm Fooshee, Daniel Willard, Jr., Gerald Hughes, William A. W. Stewart, Harry L. Umbarger, Erskine R. Myer, James B. Alley, C. C. McChord, C. M. Clay, W. Meade Fletcher, Jr., Arthur A. Gammell, W. C. Roper, Jr., H. Struve Hensel, Frederick W. Wood, Rodney J. Bardwell, Jr., H. H. Larimore,* and *Russell L. Dearmont,* for interveners.

REPORT PROPOSED BY M. S. JAMESON, EXAMINER

The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company, hereinafter referred to as the Denver and the Salt Lake Western, or the debtor and the secondary debtor, respectively, on November 1, 1935, filed petitions with the District Court of the United States for the District of Colorado, stating that they were unable to pay their debts as they matured and that they desired to effect a plan of reorganization under section 77 of the act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. On the date of the filing of the petitions the court entered orders approving the petitions as properly filed, and, among other things, pending the appointment of trustees, authorized and directed the debtor to operate and maintain both properties, under the supervision of the court. Copies of the petitions and the orders thereon have been transmitted to the Commission by the clerk of the court. In like manner the Commission has received lists of all known creditors and stockholders of the debtors, together with copies of orders of the court determining the time within which, and the manner in which, the claims and interests of the creditors and stockholders may be filed or evidenced, and [fol. 524] the division of creditors and stockholders into classes for the purpose of the plan and its acceptance. These and other documents, similarly received, are now of record in the proceeding before the Commission.

By order entered November 18, 1935, the court appointed Wilson McCarthy and Henry Swan trustees of the debtor, and these appointments were later ratified by division 4.

By order entered December 19, 1935, the court appointed Raymond L. Sauter trustee of the secondary debtor and this appointment was likewise ratified. Upon petition of the debtors, the court on April 29, 1936, entered an order extending the time for filing a plan of reorganization from the due date under section 77(d) of the act to and including August 1, 1936. On July 29, 1936, a "Proposed Plan of Consolidation and Reorganization as of January 1, 1937" was filed with the court and with the Commission by the debtor. The plan embraced the Denver, the Salt Lake Western, the Denver & Salt Lake Railway Company, the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company.

By provisions of section 77(d), after the filing of a plan, unless such plan is found to be *prima facie* impracticable, the Commission is required to hold public hearings thereon, at which any interested party may be heard, and to render a report and order in which it may either approve or refuse to approve a plan. The plan approved may be different from any which has been proposed but it must, in the opinion of the Commission, among other things, be fair and equitable, afford due recognition to the rights of each class of creditors and stockholders, not discriminate unfairly in favor of any class of creditors or stockholders, conform to the law of the land regarding the participation of the various classes of creditors and stockholders, and be com- [fol. 525] patible with the public interest. After due notice, hearings were held in October, 1936, and in February, April, and June, 1937. At the hearing on June 15, 1937, a plan of reorganization embracing the companies covered by the debtor's plan was filed by the Insurance Group committee, an intervener, of which George S. Van Schaick was chairman. Besides this group the interveners included the trustees under certain mortgages, the Untermyer family group, the Security Research Bureau, the Chase National Bank of the City of New York, the Railroad Credit Corporation, the Reconstruction Finance Corporation, hereinafter called the Finance Corporation, and others. Briefs were filed.

Classes of Creditors and Stockholders

The district court, by order entered November 23, 1936, divided the claims and interests of the creditors and stockholders as follows: Class 1, common stock; class 2, preferred

stock; class 3, claims entitled to priority under section 77 (i); class 4, claims which would have been entitled to priority over existing mortgages or other liens if a receiver in equity had been appointed for the property; class 5, claims not included in classes 3 and 4, which are entitled to priority by virtue of the laws of any State or of the United States; class 6, bonds issued under the consolidated mortgage of the Denver & Rio Grande Railroad Company dated July 15, 1886, assumed by the debtor; class 7, bonds issued under the first-trust mortgage of the Rio Grande Western Railway Company, dated July 1, 1889, assumed by the debtor; class 8, bonds issued under the first consolidated mortgage of the Rio Grande Western Railway Company, dated April 1, 1899, assumed by the debtor; class 9, bonds issued under the first mortgage of the Rio Grande Junction Railway Company dated December 1, 1889, as-
[fol. 526] sumed by the debtor; class 10, bonds issued under the debtor's refunding and improvement mortgage dated February 1, 1924, and bonds issued under the improvement mortgage of the Denver & Rio Grande Railroad Company, dated June 1, 1888, which may be held to be pledged, under the aforesaid refunding and improvement mortgage; class 11, bonds issued under the debtor's general mortgage dated February 1, 1924, and bonds issued under the improvement mortgage of the Denver & Rio Grande Railroad Company which may be held to be pledged under the aforesaid refunding and improvement mortgage; class 12, secured notes of the debtor, held by the Railroad Credit Corporation, the Chase National Bank of the City of New York, and the Finance Corporation, and debt of the Salt Lake Western, represented by the debtor's demand note which was pledged by the Salt Lake Western as security for a loan from the Finance Corporation; and class 13, all other claims not coming within any of the aforesaid specific classifications.

Claims evidenced by equipment-trust indentures and leases, or equipment-trust certificates secured thereby, were not classified, in view of the following provision of section 77(j):

> The title of any owner, whether as trustee or otherwise, to rolling-stock equipment leased or conditionally sold to the debtor, and any right of such owner to take possession of such property in compliance with the

provisions of any such lease or conditional sales contract shall not be affected by the provisions of this section.

The unsecured claims of general creditors at the time of filing the petitions under section 77 aggregated approximately $440,000. Many of the claims were discharged cur- [fol. 527] rently. The amoung coming within the 6-months' rule was not determined at the time of the hearing.

The amounts of stock, bonds, and secured notes outstanding will be shown in detail later.

The Properties

The Denver's principal eastern terminii are Denver and Pueblo, Colo., at each of which points connection is made with the Atchison, Topeka & Santa Fe Railway and the Colorado & Southern Railway. At Denver, connection is also made with the Chicago, Burlington & Quincy Railroad, the Chicago, Rock Island & Pacific Railway, and the Union Pacific Railroad; at Pueblo, also with the Missouri Pacific Railroad, which is the Denver's main outlet to the East.

On the west, the main line of the Denver passes through Salt Lake City and terminates at Ogden, Utah. Connection is made with the Union Pacific at each point; at Salt Lake City the Denver also connects with the Western Pacific Railroad and at Ogden with the Southern Pacific. The interchange with the Western Pacific is more important than that with any other Western connection.

The road owned by the Denver consists of 1,256.6 miles of main line and 1,094.9 miles of branch lines. Operated under lease are the Rio Grande Junction Railway (hereinafter called the Junction) extending from Rifle to Grand Junction, Colo., 62.1 miles, the Goshen Valley Railroad, a branch line 8.8 miles in length, and the Salt Lake Western, extending from Dotsero, on the Denver, to Orestod on the Denver & Salt Lake Railway (hereafter called the Salt Lake), 38.1 miles. Including these leased lines, the Denver operates approximately 1,357 miles of main lines and 1,104 miles of branch lines. Approximately 771 miles of narrow-gage lines are included in the operated mileage.

[fol. 528] In addition to the above-mentioned mileages, the Denver operates over the Salt Lake, between Denver and Orestod, 128.6 miles. This line, together with the Salt Lake Western, constitutes the Dotsero cut-off route. The

Salt Lake's ownership embraces the line extending from Utah Junction, near Denver, to the western terminus at Craig, Colo., 220.2 miles. For its Denver terminal, the Salt Lake uses, under a lease, the facilities of the Northwestern Terminal Railroad Company. The Salt Lake derives no revenues from the through traffic moving over the cut-off, since all such traffic is handled by the Denver.

The present Denver company was organized on November 17, 1920, succeeding The Denver and Rio Grande Railroad Company, organized in 1908. The former corporation acquired the property of the Rio Grande Western Railway Company (hereinafter called the R. G. Western), owning the line extending west from Crevasse, Colo., to Ogden, Utah, and that of the Denver & Rio Grande Railroad Company of 1886, owning all lines east of Crevasse except the Junction line. The 1908 company assumed obligation in respect of bonds issued under the R. G. Western's first trust mortgage of 1889 and its first consolidated mortgage of 1899. It likewise assumed obligation in respect of bonds issued under the first-consolidated mortgage made by the Denver & Rio Grande of 1886.

The Denver of 1908 also assumed the obligations of the predecessor companies with respect to securities issued by the Western Pacific Railway Company. It also issued bonds under new mortgages, viz, the first and refunding mortgage and the adjustment mortgage. Default in the payment of interest on the first-mortgage bonds of the Western Pacific led to a deficiency judgment against the Denver of 1908 and ultimately to the creation of the present Denver Company, which assumed obligation for all the [fol. 529] bonded debt of the former company. It issued 300,000 shares of capital stock to the Western Pacific Railroad Corporation, a new company formed for the purpose of controlling the Western Pacific Railroad Company. See *Stock of Denver & Rio Grande Western R. R.*, 70 I. C. C. 102. Later, a half interest in this stock was sold to the Missouri Pacific Railroad Company for $9,000,000. *Acquisition of D. & R. G. W. Common Stock*, 90 I. C. C. 161.

Operation of the Junction property under lease began in 1890 and continues under the same lease. It originally provided for the guaranty of the Junction's first-mortgage bonds of 1889 by the Denver of 1886 and the Colorado Midland Railway Company. The latter ceased operation in 1918. These bonds constitute an obligation of the present

debtor, which owns $906,000 of the Junction's refunding bonds, issued in 1929, and $2,000,000, par value, of the Junction's capital stock. The Insurance Group committee contends that the Junction lease is subject to the direct lien of the first consolidated mortgage of the Denver of 1886, and that the earnings of the Junction should be allocated accordingly. The debtor owns the entire capital stock of the Goshen Valley, having a par value of $50,000.

Foreclosure proceedings were instituted against the Denver in 1922 as a result of default in the payment of interest on the first and refunding mortgage and the adjustment mortgage bonds, issued in 1908, which were undisturbed in the previous reorganization. A receiver was appointed and the property was sold at auction to the reorganization managers in accordance with the plan of June 15, 1923. By deed dated December 1, 1924, the property was conveyed back to the company. See *Denver & Rio Grande Western Reorganization*, 82 I. C. C. 745 and 90 I. C. C. 141. The aforesaid first and refunding mortgage bonds, purporting to [fol. 530] represent a lien on a substantial amount of equipment, were exchanged 60 percent in new general-mortgage bonds and 40 percent in preferred stock.

The Salt Lake was incorporated on November 3, 1925, and on January 1, 1927, acquired the properties of the Denver & Salt Lake Railroad Company at foreclosure. *Denver & Salt Lake Reorganization*, 117 I. C. C. 397.

The latter company had by similar means acquired the properties of the Denver, Northwestern & Pacific Railroad Company in 1913, and had extended the line from Steamboat Springs to Craig, approximately 41 miles. Due to difficult operating conditions, the carrier went into receivership in 1917. Between that time and the reorganization of 1925-26, the Moffat Tunnel project was conceived and was carried out by The Moffat Tunnel Commission, which manages the property of the Moffat Tunnel Improvement District. The tunnel is 8.9 miles in length and the portion built for railroad use is leased to the Salt Lake. Under the terms of this lease the Salt Lake is obligated to pay 66 2/3 percent of the principal amounts of bonds issued by the tunnel commission as and when they mature.

With the purpose of developing a western outlet, the Salt Lake organized the Salt Lake Western, which completed the construction of its line from Bond (near Orestod) to Dotsero on June 15, 1934, pursuant to the certificate

issued by the Commission in *Construction by Denver & S. L. W. Ry. Co.*, 154 I. C. C. 51 and 175 I. C. C. 535. All the capital stock of the Salt Lake Western was owned by the Salt Lake. Along with the granting of authority for the construction of the Salt Lake Western line, the Commission authorized the Denver to acquire control of the Salt Lake by purchase of capital stock; *Denver & S. L. Ry. Co. Control*, 170 I. C. C. 4, and 175 I. C. C. 542. Later, in *Denver & R. G. W. R. Co. Operation*, 189 I. C. C. 129, it authorized the Denver to operate the line of the Salt Lake Western under lease and to operate, under trackage rights, over the line of the Salt Lake between Utah Junction and Orestod. The agreements made by the carriers in respect of these matters are described in 175 I. C. C. 535, *supra*. The agreement relating to the Salt Lake Western provides that, contingent upon the transfer of that company's stock or mortgage bonds to the Denver, the latter would finance the construction of the cut-off. The terms of the lease were also set forth. In accordance with this agreement, $3,631,000, par value, of the stock of the Salt Lake Western was transferred to the Denver. The Salt Lake Western has issued no bonds.

The total amount of stock of the Salt Lake acquired by the Denver is 49,540 shares, of no-par-value. Stock remaining outstanding in the hands of the public aggregates 460 shares. All the stocks of the Salt Lake and the Salt Lake Western owned by the Denver, together with various other securities, are pledged with the Finance Corporation as collateral security for loans for the financing of the construction project, the acquisition of the Salt Lake stock, and the payment of interest, taxes, and maturing equipment-trust certificates.

The investment in road and equipment of the several corporations, as shown on the consolidated balance sheet of December 31, 1936, was as follows: $211,635,295 for the Denver, $5,328,626 for the Junction, $3,659,578 for the Salt Lake Western, $503,890 for the Goshen Valley, and $17,059,350 for the Salt Lake, a total of $238,186,739. Including all investments, the grand total was $240,145,360. As of December 31, 1935, the grand total was $238,750,511. [fol. 532] In connection with the above-stated amounts appearing on the consolidated balance sheet, the debtor introduced an analysis of capitalizable assets, based on data furnished to the Commission in other proceedings in connection with applications for authority to issue secu-

rities. The result arrived at is $241,295,293, which is described as the grand total capitalizable investment as of December 31, 1935.

The report of the Bureau of Valuation dated March 1, 1937, filed in this proceeding by direction of division 4, sets forth various elements of rate making value in respect of the Denver property and that of its subsidiaries, as of December 31, 1935. For the Denver, the original cost is $142,800,512, the cost of reproduction new $168,729,747, the cost of reproduction new, less depreciation, $115,467,756, the value of lands and rights $5,428,159, and the amount of working capital $2,473,400. For the Salt Lake the corresponding amounts are $17,549,593, $19,934,420, $14,462,618, $91,854, and $287,000. For the Junction (omitting working capital) the amounts are $3,401,673, $4,100,037, $3,409,074, and $60,330, for the Goshen Valley $499,441, $308,078, $270,756, and $1,908, and for the Salt Lake Western $3,547,081, $3,920,258, $3,880,723, and $7,219, respectively. The totals for the system are: Original cost, $167,798,300; reproduction cost new, $196,992,540, reproduction cost new, less depreciation, $137,490,927; land and rights, $5,589,470; and working capital, $2,760,400.

The sum of the last three amounts is $145,840,797, and if net additions and betterments during 1936 be added thereto, the total would be $147,717,268. On the basis of original cost, the total, as of December 31, 1936, would be $178,024,641.

Securities of the Denver which are owned by the Western Pacific Railroad Corporation include 150,000 shares (50 per cent) of no-par common stock, $2,070,000, par value, of [fol. 533] preferred stock, $1,690,000 of refunding and improvement mortgage bonds, $3,751,875 of general mortgage bonds, $364,000 of R. G. Western first consolidated mortgage bonds, and $10,000 of the first consolidated mortgage bonds of the Denver of 1886. Most of these securities are pledged, the Denver's common stock being deposited with the Finance Corporation as security for a loan to the Western Pacific Railroad Company.

Securities of the Denver which are owned by the Missouri Pacific include 150,000 (50 percent) shares of the no-par common stock, $608,800, par value, of the preferred stock, and $1,000,000 of refunding and improvement mortgage bonds. All the common and preferred stock is pledged with the Railroad Credit Corporation.

Proceedings for the reorganization of the Western Pacific and the Missouri Pacific under section 77 are pending before the Commission and the courts.

Present Capital Structure.

The Denver's balance sheet of December 31, 1936, shows common stock (300,000 shares) as $62,457,540, preferred stock $16,445,600, funded debt unmatured $76,707,500, trustees' certificates $650,000, and grants in aid of construction $800,313. Total current assets were $8,025,321 and total current liabilities were $69,729,998, the latter including $12,966,372 of interest matured unpaid and $45,317,500 of funded debt matured unpaid. Corporate surplus was shown as a deficit of $2,309,419 in liabilities.

The debtor's common stock is held under a trust agreement dated February 1, 1924, voting trust certificates being held in equal amounts by the proprietary companies. The preferred stock is entitled to dividends at the rate of 6 per cent per annum, cumulative from February 1, 1924, and to $100 a share in a dissolution of the company, in preference to the common stock. No dividends have ever been paid on [fol. 534] this stock. Equipment-trust certificates were outstanding as follows: Series A, $600,000; series B, $575,000; and series C, $630,000. Pursuant to the authority granted by division 4 in *Denver & R. G. W. R. Co. Trustees' Equipment-trust certifs.*, 221 I. C. C. 291, $2,175,000 of series D certificates were issued by the trustees in 1937.

The Denver's long-term funded debt outstanding as of December 31, 1936, is briefly described as follows: Junction first-mortgage 5's, due December 1, 1939, principal amount $2,000,000, unpaid interest $158,333; R. G. Western first-trust 4's, due July 1, 1939, principal amount, $15,190,000, unpaid interest $1,215,200; D. & R. G. first-consolidated mortgage bonds, due January 1, 1936, consisting of $34,125,000, principal amount, of 4's, with unpaid interest of $3,412,500, and $6,382,000 of 4½'s, with unpaid interest of $717,975; R. G. Western first-consolidated 4's, due April 1, 1949, principal amount $15,080,000, unpaid interest $1,357,200; the Denver's refunding and improvement mortgage bonds, consisting of series A, due October 1, 1974, principal amount $2,000,000, unpaid interest $270,000, and series B, due April 1, 1978, principal amount $12,000,000, unpaid interest $1,350,000; and the Denver's general mort-

gage 5's, due August 1, 1955, principal amount $29,808,000, unpaid interest $12,544,200, of which $7,452,900 represents noncumulative interest to February 1, 1929.

In addition to the foregoing there have been issued and pledged $906,000 of the Junction's refunding 5's, $10,000 of R. G. Western first-trust 4's, $1,395,000 of R. G. Western consolidated 4's, $1,445,000 of D. & R. G. first consolidated 4's, and $10,481,000 of the Denver's refunding and improvement mortgage 5's. A statement of all securities pledged for short-term loans appears later.

[fol. 535] The debtor introduced statements setting forth its views as to what properties are subject to the respective first liens of the several mortgages. The Junction's first mortgage and refunding mortgages represent first and second liens, respectively, on the 62.1 miles of line owned by this company. No equipment is involved with these mortgages. The R. G. Western first-trust mortgage represents a first lien on 314 miles of main line and a total of 415 miles of line, together with equipment having a ledger value, less depreciation, of $17,637, as of December 31, 1936. The R. G. Western first-consolidated mortgage represents a second lien on that property and a first lien on approximately 283 miles of branch lines in Utah, the entire capital stock of the Utah Fuel Company, and equipment having a ledger value, less depreciation, of $681,191. The D. & R. G. first-consolidated mortgage represents a first lien on 875 miles of standard gauge lines and 683 miles of narrow gauge lines in Colorado and on equipment having a ledger value, less depreciation, of $4,708,523, as considered by the debtor. The Denver's refunding and improvement mortgage represents a first lien on 85 miles of standard gage and 34 miles of narrow gage branch lines in Colorado and Utah, a junior lien on all other lines owned, a collateral lien on the Junction property subject to the lien of the first mortgage, a reversionary right to the stock of the Utah Fuel Company, and a first lien on equipment having a ledger value, less depreciation, of $7,268,622, according to the debtor. In addition, there are pledged under this mortgage the shares of stock, less directors' qualifying shares, of the Denver Union Terminal Company, the Pueblo Union Depot & Railroad Company, and the Salt Lake City Union Depot & Railroad Company owned by the debtor, together with $906,000 of the Junction's refunding bonds. The Insurance Group committee contends that a portion of the above-mentioned equip-

[fol. 536] ment, having a depreciated value of $1,333,252, should be allocated to the first lien of the D. & R. G. first consolidated mortgage rather than to that of the refunding and improvement mortgage. The Denver's general mortgage represents a lien generally upon the property securing the refunding and improvement mortgage but junior thereto. The Denver's investment in the stocks and bonds of the R. G. Western, the Salt Lake, the Salt Lake Western, and the Goshen Valley, together with advances, aggregates $15,060,147. Its short-term secured debt, as of December 31, 1936, consisted of loans from the Finance Corporation totaling $10,691,850, upon which the interest unpaid amounted to $626,108, a balance of approximately $300,000 due on a loan of $500,000 from the Railroad Credit Corporation, and a demand note for $1,500,000 given to the Chase National Bank of the City of New York upon which $93,948 of interest was due.

The collateral pledged as security for the Denver's note to the Finance Corporation in the amount of $7,581,000 and the Salt Lake Western's note in the amount of $3,110,850 (the latter also secured by a demand note of the Denver for $3,182,150) consists of the following securities: $10,000 of R. G. Western first-trust 4's, $1,395,000 of R. G. Western, first-consolidated 4's, $783,000 of D. & R. G. first consolidated 4's, $4,385,000 of the Denver's refunding and improvement 5's, $1,266,000 of the Salt Lake's income 6's, 49,540 shares of the Salt Lake's capital stock, 36,310 shares of the Salt Lake Western's capital stock, 56,700 shares (100 percent) of the capital stock of the Denver-Colorado Springs-Pueblo Motor Way, Incorporated, 1,352 shares (100 percent) of the capital stock of Rio Grande Motor Way, Incorporated, 500 shares (100 percent) of the capital stock of the Goshen Valley Railroad Company, and $1,777,000 of bonds of the Rio Grande Southern Railroad [fol. 537] Company. The above-stated shares of the motor companies' stock include additional shares deposited in May, 1937, in accordance with the supplemental certificate issued by division 4 in *Denver & R. G. W. R. Co., Reconstruction Loan*, 221 I. C. C. 107. The notes to the Finance Corporation are further secured by a junior lien on the collateral pledged with the Railroad Credit Corporation and the Chase National Bank, viz, $662,000 of D. & R. G. first consolidated 4's and $6,096,000 of Denver's refunding and improvement 5's, respectively. The Credit Corpora-

tion is further secured by pledge of the debtor's distributive share of the funds collected under the "marshaling and distributing plan" and by a junior lien on the collateral pledged with the Finance Corporation. The motor companies above referred to represent an investment of $172,300 by the Denver. Operating as feeders to the railroad, they report substantial earnings in practically every year since 1927.

Unsecured general claims against the debtor aggregate approximately $440,000. An undetermined amount falls within the 6-months' rule. To the extent these unsecured creditors are not paid off currently they would be offered, under the debtor's plan, participating preferred stock at the rate of one share for each $100 of claims.

The debtor stated that during the 11-year period following the previous reorganization, more than $30,000,000 was expended for additions and betterments on the property, while the amount of equipment obligations was reduced by $1,925,000 and the amount of refunding and improvement mortgage bonds outstanding was increased by $12,000,000, due, however, chiefly to the retirement of bonds matured on June 1, 1928. For the payment of interest and taxes not earned in 1931, 1932, and 1933, loans of $3,950,000 from the Finance Corporation and of $500,000 from the [fol. 538] Railroad Credit Corporation were obtained. Additional loans from the Finance Corporation, in the amounts of $3,631,000 and $3,110,850, were obtained for the Salt Lake Western construction and the purchase of Salt Lake stock, respectively. The bank loan of $1,500,000 was also applied to the latter purpose. Including $1,042,559 of Salt Lake income bonds, together with advances, the Denver's investment in the cut-off route amounts to $12,526,376.

Division 4, by orders entered on January 29 and December 23, 1937, and March 1, 1938, authorized the trustees of the debtor to issue and sell trustees' certificates of series C, not exceeding $1,800,000 in amount, series D, not exceeding $3,200,000, series E, not exceeding $1,800,000, and series F not exceeding $2,000,000. *Denver & R. G. W. R. Co. Trustees' Certificates*, 217 I. C. C. 796, 224 I. C. C. 336 and 596.

The Denver's obligation in respect of the securities of the three terminal companies, mentioned above in connection with the refunding and improvement mortgage bonds, is shown in the agreements made for joint use of the ter-

minals. Copies of such agreements, together with the balance sheets and income accounts of the terminal companies, are of record herein.

The unpledged securities owned by the debtor and its subsidiaries include $46,000 of certificates issued by the receiver of the Rio Grande Southern Railroad Company and $850,000 of United States Treasury bonds. The debtor states that these were the only securities in the list which had any realizable value. The treasury bonds have passed out of the debtor's possession.

In connection with the Denver's reorganization of 1924 there are still issuable $108,900 of general-mortgage bonds and $15,600 of preferred stock in exchange for old securities. There are issuable by the Salt Lake, in connection [fol. 539] with its reorganization plan of 1925, approximately $20,200 of bonds and 30 shares of stock, and $21,806 in cash is being held for payment to non-assenting bondholders of the predecessor company.

As has been stated, the capitalization of the Salt Lake Western consists of common stock, all of which is owned by the debtor. The securities of the Salt Lake outstanding consist of 50,000 shares of common capital stock of no-par-value, of which 49,540 shares are owned by the debtor, and $12,500,000 of funded debt unmatured. The latter amount is composed of $1,500,000 of first-mortgage 4-percent bonds, due January 1, 1950, and $11,000,000 of 6-percent income mortgage bonds due January 1, 1960, of which $1,266,000 are owned by the debtor.

The $2,217,000 of first-mortgage 5-percent bonds of the Northwestern Terminal Railroad Company are involved to the extent that under the terms of the lease the Salt Lake pays a portion or all of the interest on such bonds, according to the amount of the railway revenues, and in the event the Salt Lake is consolidated with any other railroad the new company shall pay the full 5 percent interest. However, the debtor's plan proposes that the use of these terminal facilities be discontinued and that the debtor's terminal facilities in Denver will be used by the carriers proposed to be consolidated.

Combining and summarizing the capital structures of the debtor and its subsidiaries as of December 31, 1936, and omitting intercompany holdings and securities pledged, the total long-term and short-term debt, including unpaid interest, was $157,056,723, the amount of preferred stock

was $16,445,600 par value, and the common stock outstanding consisted of 300,460 shares, of no-par-value. The total amount of fixed interest charges for this capital- [fol. 540] ization was $5,835,392 per annum, the contingent interest charges $584,040 per annum, and the preferred stock dividend requirements $986,736 per annum, all based on the principal amounts outstanding, without consideration of the $14,293,464 of accumulated unpaid interest on secured obligations and the $12,745,240 of accumulated dividends on the preferred stock.

Subsequent to December 31, 1936, the capital structure was changed by the issue of additional equipment-trust certificates and trustees' certificates, as has been shown, and by the further accumulation of unpaid interest on funded debt and loans.

The debtor presented a pro forma balance sheet for the combined companies as of December 31, 1936, based on their present investments, with intercompany eliminations and adjustments. The capital liabilities shown are those proposed in the debtor's plan. According to this set-up the assets of the new company would consist of total investments of $228,541,993, total current assets of $9,400,095, total deferred assets of $8,495, and total unadjusted debits of $1,443,351. On the liability side, the total capitalization is shown as $119,454,419, including the proposed no-par participating preferred stock at $1 a share. The amount $113,298,420 is set up as reorganization adjustment of capital, bringing the total capital liabilities to $232,752,839. Total current liabilities are $4,277,141, total deferred liabilities $363,210, and total unadjusted credits $2,000,744. Because of the reorganization adjustment made, no corporate surplus appears.

Traffic and Earnings

As shown by traffic density charts for the years 1935 and 1936, the Denver's freight traffic is fairly uniform in total amount between Denver and Walsenburg, between Pueblo [fol. 541] and Dotsero, between Dotsero and Helper, and between Helper and Salt Lake City, the density increasing in this order of districts. East of Helper the movement is predominantly eastbound, and between Helper and Salt Lake City predominantly westbound. Most of the coal tonnage, constituting the largest single item of traffic handled, originates around Helper and moves west. Except

on small portions of line the traffic of the narrow-gage lines is generally less than 50,000 net ton-miles per mile of road a year. Of the total through traffic in 1935, approximately 40 percent moved over the cut-off. Some of this traffic was created by the opening of the new route and therefore does not represent an actual diversion from the old route via Pueblo.

Of the Denver's freight revenues in 1936, 19 percent was derived from products of agriculture, 6 percent from products of animals, 29 percent from products of mines, 6 percent from products of forests, 34 percent from manufactures and miscellaneous, and 6 percent from less-than-carload freight. The commodities constituting the chief items of traffic move, in general, over all the lines. The traffic originating on the principal branches was described in detail. Compared with the revenues of 1929 the largest relative declines have been in the products of mines and in less-than-carload freight. Compared with 1932, the total revenues in all main freight groups have increased, particularly in products of mines and forests, in manufactures and miscellaneous, and in less-than-carload freight.

The Denver's total carload traffic decreased from 330,250 cars in 1929 to 185,111 cars in 1933, then increasing each year to a total of 276,968 cars in 1936. The overhead or bridge traffic handled during the year ended June 30, 1935, aggregated 1,402,477 tons, yielding revenues of $3,754,924. [fol. 542] In the opinion of the debtor, four or five years will be required for the full development of the cut-off route. The traffic handled over it is highly competitive in character.

A record of the Denver's interchange of freight with its principal connections, from 1924 to 1935, shows that the tonnage received from the Western Pacific exceeds that received from any other line, while the tonnage delivered to the Missouri Pacific exceeds that delivered to any other. In the reverse movement these roads are also important connections. A large tonnage of freight is interchanged with the Union Pacific and Southern Pacific. The Denver's interchange with the Salt Lake is small compared to the interchange with the trunk lines.

Traffic reported as being handled by the Denver, following the opening of the cut-off route, includes that handled over the lines of the Salt Lake Western and the Salt Lake

under the operating agreements made with those carriers, but does not include that handled in trains operated by the Salt Lake.

Of the total freight revenues of the Salt Lake in 1936, approximately 61 percent was from the traffic in bituminous coal. Other important items were crude oil, gasoline, and cement. The coal originates at several local stations and is hauled principally to Denver. Mines are numerous in the territory served. The number of carloads handled in 1936 exceeded that of any previous year. The same is practically true of the oil and gasoline. The latter originates at Craig and is shipped to Denver, and to points west via the cut-off. The Salt Lake's total carload traffic decreased from 32,014 cars in 1929 to 15,801 cars in 1933, then increasing each year to a total of 35,213 cars in 1936. The number of carloads delivered to connecting carriers in 1936 was 24,207 and the number received from such carriers was 1,288.

[fol. 543] The opening of the Moffat Tunnel in 1928 was followed by a marked increase in the earnings of the Salt Lake, and a further increase followed the opening of the cut-off route on June 15, 1934, due to the rentals paid to the Salt Lake by the Denver. The latter's net railway revenues, however, were reduced. Considering the operation of all lines involved, the net loss due to the cut-off, for the 12 months ended June 30, 1935, was computed at approximately $218,000 on the way-bill method of allocating revenues adopted by the debtor, allowing a constructive mileage to the cut-off, or at approximately $285,000, on the way-bill basis, allowing the cut-off its actual mileage. The methods used for allocating revenues will be explained in connection with the plans filed.

The Denver's total operating revenues were at a maximum of $34,828,669 in 1929, declined to less than half that amount in 1933, and have increased progressively since that year, reaching $25,599,309 in 1936 and $8,180,745 during the first four months of 1937. Net railway operating income, however, did not change proportionately, having amounted to $8,528,676 in 1929, $3,357,643 in 1933, and $1,569,814 in 1936. This decline may be ascribed to the steady increase in operating expenses, taxes, and joint facility rents. The emergency freight surcharges collected in 1932 and 1933, under the authority of the Commission in Ex parte 103, amounted to $380,862, and during 1935 and 1936, under Ex

parte 115 to $547,167. Wage reductions made under agreements with organized labor amounted to $851,780 in 1932, $876,876 in 1933, $872,996 in 1934, and $118,024 in 1935. Wages were fully restored on April 1, 1935. The estimated amount of the charges to tax accruals in 1936 on account of the Federal Railroad Retirement Act was $403,479 and on account of the Social Security Act, $135,017.

[fol. 544] The Denver reported a nonoperating income of $675,615 in 1935 and $709,590 in 1936. An analysis of the first figure shows the principal subitems to be income from lease of road and equipment $245,241, dividends on the stock of the Salt Lake Western, $145,240, and interest on a bearer note of the Salt Lake Western, $128,372. After intercompany eliminations, the nonoperating income (including $66,320 as that of the Salt Lake in the same year) amounted to $223,081. Miscellaneous deductions from income aggregated $260,828 in 1935 and $258,547 in 1936. Income available for the payment of interest was $8,938,657 in 1929, $3,497,991 in 1933, and $2,020,857 in 1936. The net income in 1929 was $3,554,110, and the income deficits in 1933 and 1936 were $2,139,757 and $3,911,204, respectively.

The operation of the narrow-gauge lines is reflected in the foregoing figures. About 88 percent of the net ton-miles of these lines is within the territory subject to the lien of the D. & R. G. first consolidated mortgage. The system revenues contributed by the traffic handled from and to points on these lines aggregated $1,953,000 in 1934 and $2,017,000 in 1935. The debtor considers that the system revenue derived from the freight traffic originated on the narrow-gauge lines about equals the operating loss on such lines.

During the three years ended June 30, 1935, the income of the Denver available for the payment of interest represented approximately 1.12 percent of the average book investment in road and equipment, less accrued depreciation on equipment.

The total operating revenues of the Salt Lake declined from the high level of $3,981,131 in 1929 to the low of $1,620,006 in 1934, increasing to $2,234,882 in 1935, and to $2,856,949 in 1936. The corresponding net revenues [fol. 545] from railway operations were $1,754,484, $805,155, and $918,281, and the net railway operating income $1,679,287, $913,122, and $1,090,810. The emergency freight surcharges on the Salt Lake amounted to a total of $119,121

during the years 1932, 1933, 1935, and 1936. The wage reductions aggregated $50,863, the charges under the Railroad Retirement Act $50,037, and those under the Social Security Act, $17,542. The Salt Lake reported net income of $610,069 in 1929, $12,493 in 1934, and $2,455 in 1936.

The combined income accounts of the Denver and the Salt Lake for the years 1927 to 1936, inclusive, with adjustments for intercompany charges and credits, and for an error appearing in the account for 1935, show a downward trend in the income available for interest from 1929 to 1932, a fairly constant level between 1932 and 1935, when it averaged about $3,600,000 a year, and $2,417,746 available in 1936.

The reports of the Bureau of Accounts, filed in this proceeding by order of division 4, show the result of corrections in the carriers' income accounts, 1930 to 1934, inclusive, for accounting not in accordance with the Commission's regulations, an adjustment to include income items entered in profit and loss account by permission of the Commission, and a further adjustment to give retroactive effect to the excise tax in connection with the Railroad Retirement Act, effective March 1, 1936, the Social Security Act, effective January 1, 1936, and the Commission's order respecting accounting for equipment depreciation, effective January 1, 1935. The combined effect of these changes is to reduce the average income of the Denver, available for the payment of interest, from $4,243,563 per annum, to $3,521,239 per annum during the period. On the same basis the average available income of the Salt Lake is reduced from $655,771 per annum to $540,395 per annum.

[fol. 546] Although the combined gross revenues of 1936 were substantially in excess of those of 1935, the net revenues were less, largely because of the heavy maintenance program. Maintenance of way expenditures for the system increased from $2,752,695 in 1935 to $4,453,359 in 1936; maintenance of equipment from $5,285,329 in 1935 to $7,215,066 in 1936, notwithstanding the abnormally high maintenance expenditures in 1935 as reflected in the adjustments made by the debtor in the earnings for the year ended June 30, 1935, hereinafter discussed. On the Denver in 1936, operating expenses were charged with $836,614 in connection with capital charges of $1,314,392 for roadway.

On the Salt Lake, the corresponding charges were $248,005 and $668,574.

In 1936, the Denver expended approximately $1,200,000 on maintenance of way work deferred from prior years and in connection with improvements. For maintenance of equipment $800,000 was spent under like requirements. The Denver proposed an improvement program for the years 1937, 1938, and 1939, involving a total capital expenditure of $6,179,700 for road and equipment, with operating charges of $4,070,800, and cash requirements of $9,905,200 in connection with such improvements.

The Salt Lake's line has been largely rebuilt during recent years and the amount of deferred maintenance is evidently slight. A witness for the Finance Corporation considers the line to be virtually a new railroad. However, an improvement program for the years 1937, 1938, and 1939 is contemplated, by a director of the Salt Lake, under which the expenditures would be $2,194,000 for road and equipment and $693,000 for operating expenses. More than half this outlay would be made for reducing curvature and revising the alinement. The debtor's testimony was to the effect [fol. 547] that the expenditures for improvements would have to be continued for two or three years longer in order to bring the Salt Lake up to the standard of the Denver. Incidental to the showing made by the Finance Corporation with respect to the Salt Lake, a study was introduced in which the income available for interest was estimated at $1,449,000 for 1936 on the basis of the Salt Lake's operation as an independent carrier, assuming no further rehabilitation of the line between Orestod and Denver to be necessary.

A study for a determination of the earnings of the Denver and the Salt Lake during a normal year was presented by the president of the Denver, such study indicating that the total operating revenues of both roads would be $33,721,189, the total operating expenses $23,918,282 (operating ratio 71.49 percent), the net railways operating revenue $6,435,857, and the income available for interest $6,215,423. In the opinion of the witnesses such results may be expected in 1939. The debtor's estimate of freight traffic, which was made in collaboration with the officers of two trunk lines that connect with the Denver, was based on a study of the traffic in each principal commodity handled between 1928 and 1936, and the number of carloads, average tonnage, and average revenue per car for a normal year were estimated in the case of each commodity. Consideration

was given to business conditions in the local territory and to the trend of production, to the effect of opening the cut-off, and to present and prospective rate levels. A substantial increase in the traffic connected with the mining industry is reflected in the forecast. Operating expenses were based on the total amount of revenues estimated. A continuation of the present scale of wages was assumed. Maintenance expenses for the Denver were fixed at 33 percent of [fol. 548] gross revenues, which compares with an average of 35 percent for the years 1925 to 1936, inclusive. For the Salt Lake, the ratio was taken at 30.7 percent.

A study of the prospective revenues of the combined lines was also made by a bank officer, testifying as a financial expert, who showed that the operating revenues of the Denver since 1933 represented an increasingly large proportion of the operating revenues of all class I roads. By relating the trend of railroad earnings to the number of workers employed in the durable goods industries, and making certain assumptions as to normal conditions in industry and in railroad rates, the witness arrived at an estimate of $32,559,560 for the total operating revenues of the Denver. Such sum is $1,825,560 in excess of the "normal" revenues shown in the president's forecast.

The debtor selected the 12 months ended June 30, 1935, as the basis for the allocation of earnings to mortgage districts in connection with the development of its plan of reorganization. In this so-called test period, the total operating revenues of the system were $21,828,298, the total operating expenses $16,485,571, the net railway operating income $3,149,365, and the income available for interest $2,923,024.

These figures, however, were materially changed, as will be shown in describing the debtor's plan, by adjustments made in order to eliminate abnormalities in operating conditions during the test period and to establish a level of earnings which would be generally representative, giving effect to the opening of the cut-off route. Thus, the income of the Denver assumed as available for interest was increased to $2,813,063, and by adding the earnings of the Salt Lake's independent operation, together with the estimated savings for unified operation, the system income available, [fol. 549] based on the test period year, was placed at $3,926,223. This was the figure used in computing the amounts of new bonds assignable to the present first-lien

bondholders on the basis of the respective earnings of different divisions of the system, but in the determination of the amount of future fixed charges permissible still another change of base was introduced, viz, the average earnings of 1932, 1933, and 1934. With certain adjustments, this computation indicated $3,687,328 as the income of the system available for the payment of interest.

Debtor's Plan of Reorganization

The debtor's plan, dated July 28, 1936, is based upon a consolidation of the properties of the Denver, the Salt Lake, the Salt Lake Western, the Junction, and the Goshen Valley. The amount, character, and distribution of securities to be issued by the new company were determined primarily from earnings. During the course of the hearing the debtor, at the request of certain interveners, made additional studies of the earnings of the lines subject to first-lien mortgages, arriving at a distribution of the new securities which differed materially from that originally proposed. On brief, the revised distribution is favored, yet the debtor states that it does not desire technically to amend the original plan.

In order to ascertain the earnings of the several mortgage districts as a basis for the apportionment of new bonds, the debtor adopted a formula or general method, which was applied to the revenues and expenses of the Denver during the 12 months ended June 30, 1935. The Salt Lake was not included in the first step of the analysis since its mortgages apply to the entire line and its earnings are separate from those of the Denver. Freight revenues of the Denver were divided among the mortgage districts on an average ton-mile basis, and it was considered proper to assign the [fol. 550] same mileage to the cut-off route between Denver and Dotsero as that of the old route between those points via Pueblo, although the latter route is approximately 175 miles longer.

It appears from the revised figures, as has been stated, that the operation of the cut-off during the first year resulted in a system loss of approximately $218,000, because of increased transportation costs, despite a substantial increase in through traffic. The effect of the diversion of traffic to this route was to deprive the lines subject to the lien of the D. & R. G. first consolidated bonds of approxi-

mately $900,000 of annual revenue, which would otherwise have accrued to such lines.

Maintenance of way expenses were adjusted in a manner intended to show normal conditions over an average period. For the cut-off, much larger expenses than the actual were used. Maintenance of equipment expenses were apportioned to engine districts on the basis of equipment mileage, using the years 1933 and 1934 as typical, and certain assumed ratios were employed in dividing the total expense of locomotive repairs between the freight and passenger services.

For the use of equipment, the charges to each first-lien mortgage were made on the basis of 2 percent per annum applied to the ledger value of the equipment used, less depreciation. The mortgage with a lien on the most equipment represented the district where the smallest use of equipment took place. In support of the 2-percent rate, the debtor cited the interest rates on various recent equipment trust issues. Yard switching expenses were distributed on a car-mile basis over the different divisions of the system. This method was also followed for maintenance expenses of yards and yard locomotives, station services, etc.

[fol. 551] The adjustments made in the actual earnings of the Denver during the test-period year consisted principally of a reduction of approximately $714,000 in total maintenance charges, a reduction of $452,618 in nonoperating income, due to intercompany eliminations, of which reduction $65,889 was not specifically explained, and the elimination of $261,570 of miscellaneous deductions from income, of which $10,807 was not explained. To the income of the Denver there were added $182,342 to compensate for the abnormally low earnings from the potato traffic originating in the San Luis Valley, and $83,333 to represent the earning power of the Utah Fuel Company. As a result of all adjustments, the income of the Denver available for interest was finally shown as $2,813,063, and the corresponding amount for the consolidated system as $3,926,223.

Objections to the use of the year ended June 30, 1935, as an earnings base were expressed by the trustee of the R. G. Western consolidated mortgage, the trustee of the Denver's refunding and improvement mortgage, the Untermyer family group, and the Security Research Bureau. In

general, these interveners urge the use of a base reflecting conditions after the cut-off route shall have become definitely established.

The entire formula is admittedly open to objection and is largely a matter of judgment. Controversy arose especially in regard to the debtor's treatment of the cut-off, the priority of mortgage liens with respect to equipment, the rental charged for equipment, the segregation of company freight, the allocation of branch-line losses, the adjustment for the higher rate scale on the narrow-gage lines, and the period chosen as representative of earning power.

The debtor revised its first formula in various respects, principally by allocating freight revenues according to [fol. 552] actual way-bills to the extent records thereof were available, by segregating company freight and including only so much of the cost of handling as was involved where one mortgage district bore the expense of work done by another, by separating train switching from general road operation, and by charging the narrow-gage districts with the cost of transferring freight from narrow-gage to standard-gage cars, and vice versa. The test-period basis of earnings, as adjusted, was retained, but the revisions just mentioned resulted in substantial changes in the allocations.

A further revision of the formula showed the effect of computing the earnings of the cut-off operation on a straight mileage basis. This analysis was utilized in part by the committee in preparing its plan, as will be explained later.

From the primary distribution of earnings, the ratio of the earnings of each mortgage district to the total was established. These ratios were next applied to the total fixed interest charges considered permissible for the new company. In the detailed computations such charges were taken at $2,598,474, based on a 1.3 coverage for the earnings of the calendar year 1935, and in the final set-up for the new capital structure they are shown as $2,584,165. The debtor offers further support for the total fixed charges proposed by referring to the average income available for interest during the 3-year period 1932-34, which with certain adjustments, was $3,687,328, or 1.42 times the amount of the charges adopted.

After the distribution of each mortgage district of its proportionate share of the permissible new interest charges, such shares were compared with the earning power of each district, as established on the basis of the test-period per-

formance. In the case of certain districts, such as those [fol. 553] represented by the Junction first mortgage and the R. G. Western first-trust mortgage the earnings exceeded the proposed fixed interest charges; in other divisions deficiencies were shown. The surpluses were passed on to the next junior obligations, and were considered in fixing the amount of new bonds to be offered to the present bondholders, the Finance Corporation, and the Credit Corporation. The Finance Corporation, by virtue of its lien on the stocks of the Salt Lake and Salt Lake Western, was credited with the earnings of the cut-off route and those of the Salt Lake's separate operation. It was also credited with the dividends paid on the stocks of the motor carriers. From calculations based on the revised formula, the debtor arrived at new proportions for the distribution of first and refunding mortgage bonds, general-mortgage bonds, and first preferred stock to the holders of the present securities. The record of market prices of the debtor's securities was given some weight in determining the allocation of new securities.

The debtor proposes to leave the equipment obligations undisturbed, to call in the Salt Lake's bonds for redemption, to issue bonds under three new mortgages, and to issue three classes of new capital stock, all to be exchanged for existing bonds, stocks, and the notes to the Finance Corporation and Credit Corporation in varying ratios. A new collateral note would be issued to the Chase National Bank. No provision is made in the plan for the trustee's certificates which may be outstanding when the plan becomes effective. The Western Pacific and the Missouri Pacific would retain stock control of the new company but each would relinquish the $1,000,000 of refunding and improvement mortgage bonds which it owns, and in addition each would agree to purchase $1,500,000 of new bonds at par. In connection [fol. 554] with the equity in the present common stock the debtor showed that between 1925 and 1935 approximately $4,383,000 was expended for improvements from net income which might have been applied to dividends on the common stock. The cost of the improvements made on each mortgage district and on the Salt Lake was supplied for the record.

Under this plan new income bonds are to be offered for the 460 shares of Salt Lake stock outstanding in the hands of the public. The Finance Corporation was expected to

underwrite $11,443,680 of new first and refunding mortgage bonds, and to accept $11,317,950 of such bonds as payment of the debt to it.

Accruals of unpaid interest on the present bonds and short-term debt, of the Denver, excluding pledged bonds, amounted to $14,293,464 as of December 31, 1936. The debtor makes no provision for interest not earned during the trusteeship, amounting to approximately $4,770,000. Other accrued interest is to be funded in new securities junior in rank to those issued against the principal obligation.

The new capitalization proposed by the debtor, based on the obligations actually outstanding on December 31, 1936, would be as follows: Equipment-trust obligations, $1,895,000; Western division 3½-percent bonds, representing a first lien on the standard-gage lines west of Dotsero, $22,680,233; first and refunding mortgage 4-percent bonds, representing a first-lien on all standard-gage lines east of Dotsero and a second lien on all other standard-gage property, $48,222,730; general income mortgage 4-percent bonds, cumulative for two years, representing a lien junior to that of the first and refunding bonds, $18,686,850; first preferred 4½-percent non-cumulative stock, of $100 par value, $30,376,050; participating preferred 5-percent stock, of no-par. [fol. 555] value, 413,842 shares; common stock, of $1 par value, 200,000 shares; and a collateral note for $1,542,200 issued to the Chase National Bank. The bonds and stock proposed to be pledged as security for this note are not included in the foregoing totals. There is included in the amount of first and refunding bonds stated, $3,000,000 of bonds which are to be sold immediately to provide for capital expenditures, and $3,000,000 of bonds which are to be available for sale to the Missouri Pacific and Western Pacific. The debtor considers that the minimum amount needed for cash working capital is approximately $1,000,000. Approximately $277,000 in cash would be paid to the holders of certain divisional bonds as an adjustment of interest rates.

The capital stock of the Utah Fuel Company would be pledged under the proposed general mortgage. As has been indicated, this stock is now under the first lien of the R. G. Western consolidated mortgage, subject to a right of redemption upon the payment of $6,000,000 in cash or upon the deposit with the mortgage trustee of $6,000,000, principal amount, of the consolidated mortgage bonds. The

company's balance sheet of December 31, 1936, shows the asset value of the fuel company property as $15,171,943, the par value of stock outstanding as $10,000,000, and the corporate surplus as $2,652,839. An appraisal of the property, made for the trustee of the R. G. Western consolidated mortgage by a mining expert, indicated a going-concern value of $4,653,720. As has been stated, the debtor, in applying its formula for allocation of earnings by mortgage districts, credited this mortgage with an income of $83,333 per annum from the fuel company, based on dividends paid, but not earned, in the period 1932-34. In 1935 and 1936, small amounts of net income were reported. The [fol. 556] property and its operations are completely described in the record. As part of the security for the R. G. Western consolidated mortgage bonds, its value is an element in the claims of the trustee under that mortgage.

Including $1,865,000 of equipment obligations and $650,000 of trustees certificates, the total funded debt of the new company under the debtor's plan would be $92,937,013, the fixed interest charges $2,868,235 per annum, and the contingent interest charges $747,474 per annum. Dividend requirements on the first preferred stock would be $1,366,922 and on the participating preferred $2,069,210 per annum. The total capitalization of the new company, if a par value of $1 a share be assigned to the participating preferred stock, would be $123,926,905.

The theoretical application of income available for interest annually would be in the following sequence, under the debtor's program: 1, Fixed interest, $2,868,235, 2, fund for additions and betterments, $350,000; 3, fund for retiring first and refunding bonds (one-half of 1 percent per annum on the maximum principal amount at any previous time outstanding) $241,113; 4, contingent interest or income bonds, $747,474; 5, second payment to the fund for additions and betterments, $250,000; 6, fund for retiring income mortgage bonds (one-fourth of 1 percent on the maximum principal amount at any previous time outstanding $46,717; 7, dividends on the first preferred stock, $1,366,922; 8, dividends on the participating preferred stock, $2,069,210; grand total before dividends on the common stock, $7,939,671.

The foregoing figures omit provision for the payment of any undistributed profits tax under the Revenue Act of 1936. The debtor submitted an estimate of the amount of such tax in the future, based on various amounts of net

[fol. 557] income available for interest, indicating $180,000 per annum as a probable maximum.

Expenditures for additions and betterments during three years after reorganization would be initially capitalized in full through the issue of not exceeding $6,000,000 of first and refunding mortgage bonds to be issued as treasury bonds. Thereafter, bonds may be issued under either the Western division mortgage or the first and refunding mortgage up to 75 percent of the cost of additions and betterments, the remaining 25 percent to be supplied through the proposed capital fund. The debtor's intention is that the first and refunding mortgage bonds shall constitute the principal medium, but not the only medium, of future financing.

The plan is the result of a comprehensive study by the secretary-treasurer of the Missouri Pacific, and was made at the request of representatives of that company and the Western Pacific, acting as a managing committee of the Denver. Conferences on the development of the plan were had with representatives of the Finance Corporation, the Chase National Bank, the insurance group, and others. Resolutions approving the plan were enacted by the boards of directors of the several companies involved, except the Salt Lake and the Goshen Valley, but no action has been taken with respect to the application for authority to consolidate the properties in accordance with section 5 (4) of the Interstate Commerce Act, as amended. The debtor contends that under the provisions of section 77 (b) applications for authority to consolidate are unnecessary.

Disapproval of the debtor's plan was expressed by the Insurance Group, the Security Research Bureau, several mortgage trustees, the Railroad Credit Corporation, the Finance Corporation, and others. The Finance Corpora-[fol. 558] tion declined to give its consent, as pledgee of the stocks of the Salt Lake and the Goshen Valley, to the concurrence of these companies in the plan. It contends that during the period of the Denver's trusteeship no rental has been paid for the use of the Salt Lake Western line, nor have the trustees acted either to affirm or disaffirm the lease.

The chairman of the Finance Corporation is in favor of a consolidation of the Western Pacific and the Denver. A special committee of the latter's directors has been appointed to negotiate such a consolidation, and in the event it is to be undertaken the debtor will file a supplemental plan. The debtor considers that the proposed Western

division mortgage might be extended to cover the Western Pacific property, and certain of the bonds reserved under that mortgage could be issued to the holders of Western Pacific securities.

The Finance Corporation introduced evidence pertaining to the cut-off route, as compared with the route via Pueblo, for the purpose of showing the superiority of the former in respect of grades, curves, and other physical features, cost of moving freight and passengers, originated traffic, and many other matters. It contends that its loans to the Denver are fully secured, that it has extensive powers of control over the Salt Lake and the Salt Lake Western, and that it is entitled to such treatment in the reorganization as will fully satisfy its claims. Objection is made to the proposed offer of new bonds which would represent only a second lien on the Western lines, and it is urged that all unpaid interest should be paid in full.

Insurance Group Plan

The Insurance Group committee represents seven mutual life insurance companies which, taken together, owned [fol. 539] $15,871,000 of bonds issued under the Denver's underlying mortgages, principally the R. G. Western and D. & R. G. first consolidated, but no bonds issued under the debtor's own mortgages. The holdings represent more than 10 percent of the principal amount of bonds in each class outstanding. These insurance companies owned more than $91,000,000 of bonds and equipment obligations of the Missouri Pacific and its subsidiary companies, and nearly $15,000,000 of similar securities of the Western Pacific.

The formula used by the committee for the distribution of revenues and expenses is a modification of the debtor's formula, based on the same test period. Consolidation of the properties is likewise contemplated, and, while consolidation with the Western Pacific is not directly provided for, the committee states that its plan leaves the way open for such consolidation.

The committee used the debtor's distribution of earnings by mortgage districts, as revised on the basis of actual way bills, adjusting the results thereof (1) by allowing 42 percent of the constructive mileage adjustment for the cut-off, (2) by reallocating a certain group of equipment, and (3) by recognizing all fixed interest charges unpaid up to

December 31, 1936. The net result of the changes was to increase the amounts of test-period earnings (totaling $3,926,223) assigned to the Junction first-mortgage, the R. G. Western first-trust mortgage, and the D. & R. G. first consolidated mortgage, and to reduce the amounts assigned to other items, notably the lines subject to the lien of the Finance Corporation notes.

The arbitrary allowed to the cut-off in the committee's plan arises from an adjustment of the debtor's ascertain-
[fol. 560] ment of unit operating expenses for the two routes, respectively, such adjustment being confined to maintenance costs, which, it was thought, the debtor had not treated on a comparable basis. Rejecting the debtor's various reasons for the 175-mile arbitrary allowed to the cut-off, the committee asserts that if the cut-off were operated as a separate railroad no division of the through rate could reasonably be expected to exceed the 42-percent allowance.

The committee's adjustment with respect to the allocation of equipment results in a credit of $26,665 to the earnings of the D. & R. G. first consolidated mortgage district and a debit of like amount to the earnings of the refunding and improvement mortgage district. This amount represents the application of the 2-percent rental to equipment having a ledger value, less depreciation, of $1,333,253, and considered by the committee to be subject to the paramount lien of the D. & R. G. first consolidated mortgage rather than to that of the refunding and improvement mortgage. As to all other equipment the debtor's allocation of equipment under the several mortgages was adopted by the committee.

This plan assigns the earnings of the Junction, in excess of the requirements of its present bonds, to the D. & R. G. first consolidated mortgage district, while the debtor assigns them to the refunding and improvement mortgage district. The point at issue is whether or not a lease agreement, made in 1889, is subject to the first consolidated mortgage by virtue of the after-acquired clause of that mortgage.

In applying its formula, the committee arranged the present mortgages in four groups, viz. the R. G. Western district, the D. & R. G. district, the R. & I. district, and the R. F. C. district, and based its computations on the total earnings allocated to each. In the case of the R. G. Western
[fol. 561] district, $16,415,667 of new first-mortgage fixed-interest bonds are to be issued for a like amount of claims

of the present first trust bonds, both actually outstanding and pledged, with all unpaid interest to December 31, 1936. This treatment recognizes the fact that the test-period earnings were in excess of the interest requirements of the first trust bonds. For the total claims of the R. G. Western consolidated mortgage bonds, the committee proposes to issue $8,938,577 of new first-mortgage bonds and $9,506,025 of new income bonds, the latter figure including $567,448 as an allowance for control of the Utah Fuel Company. The total amount of these new bonds is equal to the total amount of present consolidated mortgage bonds, with interest. This result is arrived at despite the fact that the earnings in the test-period year, allocated to the consolidated mortgage bonds, are shown as a deficit of $96,811. It further appears that, although the committee's calculations to determine the allowable amount of fixed interest and contingent interest bonds purport to reflect average earnings during the period 1932-35, the test period base has been adhered to in fact. In the brief filed by the Security Research Bureau many alleged errors in the calculations are pointed out.

The plan proposes a new first mortgage, secured by a lien on all the consolidated railroad properties, except the narrow-gage lines and their equipment, together with the stock of the Utah Fuel Company. Series-A bonds issued under this mortgage would be convertible into series B, would bear interest at 4 percent, and mature in 15 years. The reorganization committee would have the power, subject to the approval of the Commission, to reduce the term to not less than 10 years and to increase the rate of interest to not exceeding 4½ percent, in order that such bonds may be marketable at or near par. The series-B bonds would [fol. 562] bear interest at 4 percent and have a term of 40 years. The first-mortgage bonds, which may be limited in amount by the terms of the mortgage, are to be issuable to the extent of 75 percent of the cost of additions and betterments. Income mortgage bonds, subject only to the lien of the new first mortgage, would be issued under a mortgage closed at the amount of bonds to be issued in the reorganization. The income bonds would have a term of 50 years and an interest rate of 4½ percent, cumulative up to a maximum of 22½ percent. These bonds would be entitled to a sinking fund of one-fourth of 1 percent per annum on the total principal amount of bonds issued in the reorganization.

The plan proposes an issue of convertible preferred stock, entitled to dividends at the rate of 5 percent per annum, cumulative; common stock of two classes; and warrants carrying the right to purchase common stock. A new collateral note would be issued for the present bank debt, and provision is made for the issue of a promissory note to the Railroad Credit Corporation in the event the latter's note is not paid through distributions under the marshaling and distributing plan, or by cash. For the total amount of principal and interest due the Finance Corporation, approximately 58 percent is proposed to be paid in new first-mortgage bonds, series B, and 42 percent in new income bonds.

The chairman of the Finance Corporation advised counsel for the committee that if it is not found feasible to effect a consolidation of the Denver and the Western Pacific, and the plan of the committee is approved by the Commission and affirmed by the court within a reasonable time, the Finance Corporation will finance, at par and accrued interest, $11,443,675 of new first-mortgage 4-percent bonds, as provided in the plan for the purpose of refunding the first-mort- [fol. 563] gage and income bonds of the Salt Lake now outstanding.

The new capitalization proposed by the committee, based on the obligations actually outstanding on December 31, 1936, would be as follows: Equipment-trust obligations $1,805,000; first-mortgage bonds, series A, $18,563,533; series B, $52,057,197; income mortgage bonds, $27,042,895; a collateral note for approximately $1,542,200; preferred stock, $26,403,389, par value; common stock, of no-par-value, class A, 349,002 shares; warrants for class-A common stock, 164,456 shares; and warrants for class-B common stock, 200,000 shares. The above total of first-mortgage bonds includes, for the sake of comparison with the debtor's plan, $6,000,000 of bonds proposed to be issuable to redeem trustee's certificates, to provide for reorganization expenses or working capital, or to be applied to other approved purposes. Securities to be issued and pledged are not included in the above summary. Approximately $58,000 in cash would be paid to the holders of certain divisional bonds as an adjustment of interest rates.

The total amount of funded debt under this plan would be $101,359,982, the fixed interest charges $2,961,915 per

annum (assuming the interest rate on the first-mortgage series-A bonds to be 4 percent), and the contingent interest charges $1,216,930 per annum. Dividend requirements on the preferred stock would be $1,320,169 per annum. The total capitalization of the new company, assigning a par value of $1 a share to the common stock and warrants, would be $128,476,829.

The theoretical application of income available for interest annually under the committee's program would be in the following sequence: (1) Fixed interest, $2,961,915; (2) fund for additions and betterments, $750,000; (3) contin- [fol. 56] gent interest, $1,216,930; (4) sinking fund for the income bonds, $67,607; and (5) dividends on preferred stock, $1,320,169; grand total, before dividends on the common stock, $6,316,621.

Under this plan, the Junction first-mortgage bonds and the R. G. Western first trusts would receive new first-mortgage bonds in amounts equal to the principal of the present bonds, respectively, plus accrued interest. In the case of all other bonds, various proportions of first-mortgage series-B bonds, income bonds, and preferred stock are assigned, except that class-A common stock only, is to be issued for the present general-mortgage bonds, and the present bonds of the Salt Lake are to be called for redemption and paid through the issue and sale of new first-mortgage series-B bonds, as has been noted. Income bonds in the amount of $9,931 are proposed to be issued to the holders of the 460 shares of Salt Lake Stock outstanding in the hands of the public. The new class-A common stock, allocated to the holders of general mortgage bonds, is to be placed in a voting trust pending the disposal of the matter of equity in the present common stock, as hereinafter explained.

The holders of the 164,450 shares of preferred stock would be offered warrants for the purchase of a like number of shares of new class-A common at a suggested price of $20 a share. The holders of the 300,000 shares of common stock would be offered, pro rata, warrants for 200,000 voting trust certificates or shares of new class-B common stock at $30 a share, at any time within six months from the date of effectuation of the plan. In the event this option is not exercised, an assignable option, in the form of warrants, will revert to the reorganization committee for the purchase of 200,000 shares of class-B common at $30

a share, within three years from the effectuation of the [fol. 565] plan. The reorganization committee would be authorized to transfer such option to any interests that it may select as being of the greatest advantage to the new company. The committee suggests the advisability of offering part of the option to the Chicago, Burlington & Quincy Railroad Company and the Chicago, Rock Island & Pacific Railway Company, because of the importance of these connections at Denver, and it is contended that there should be no objection to this association of interests on the part of the Missouri Pacific. Representatives of the latter testified as to the established traffic relations between the Missouri Pacific and the Denver, and the possible unfavorable effect of a future alliance between the Denver and other system, such as the Burlington.

The committee's proposed treatment of the stockholders of the Denver is predicated on a finding that the equity in the present stock is without a value and that the interests of present creditors must receive full consideration before those of the stockholders. In support of its position in this matter, counsel, on brief, cite numerous opinions of the courts, including *In re New York Railways Corporation*, 82 Fed. (2d) 739, and *Northern Pacific R. Co.* v. *Boyd*, 228 U. S. 482. However, the committee, recognizing the interdependence of the Denver, the Missouri Pacific, and the Western Pacific, and the desirability of maintaining the through route which has been developed has provided in its plan the above-described means whereby the proprietors may retain control of the Denver.

Cash proceeds received by the new company from the exercise of the warrants are to be used initially to redeem income mortgage bonds issued to the Finance Corporation. The new class-A common stock would carry full voting [fol. 566] power on all matters affecting the essential aspects of its proprietary interest, while the new class-B common stock, if and when one half of such stock becomes outstanding, would be entitled to elect a majority of the board of directors of the new company, to consist of 12 members. One member would be elected by the holders of the income bonds, two by holders of the preferred stock, and two by the holders of the class-A common stock. The remaining members would be elected by the holders of the class-B common stock.

All the common stock would be issued to the reorganization committee as voting trustees, to be held by them for a period not exceeding three years, but the voting trust may be terminated within 90 days from the date of payment for the warants issuable to the reorganization committee. The reorganization committee would consist of seven members, of whom six would represent a like number of classes of present bonds, and one would be designated by the Finance Corporation.

The plan provides that it shall not be carried out until it shall have been accepted by or on behalf of the holders of at least two-thirds in principal amount of each class of the outstanding bonds of the debtor and by the Finance Corporation, nor unless either (1) the plan shall have been accepted by creditors, other than bondholders and the Finance Corporation, holding at least two-thirds in principal amount of the claims of each class and by the stockholders of each class holding at least two-thirds of the stock of such classes or (2) provision shall have been made for protecting the interests of such non-assenting classes of creditors and stockholders as provided in Article VIII of the plan, provided the reorganization committee may under certain conditions eliminate the requirement for consent as to any class of bondholders or the Finance Corporation upon [fol. 567] substituting therefor the protection for protecting the interests of the bondholders and the Finance Corporation as is provided in Article VIII as to the other classes. Article VIII provides in effect that the properties shall be sold at public auction at not less than a fair upset price as determined by the court in the event that, after the plan shall have been accepted by the holders of at least two-thirds in principal amount of each class of bonds affected by the plan, the holders of more than one-third in principal amount of any other class shall not have accepted the plan within a period to be fixed by the reorganization committee, with the approval of the Commission and the court. In the event of such sale the nonassenting creditors of such class and the nonassenting stockholders of such class shall be entitled to receive their aliquot proportion of the proceeds of such sale, after deducting therefrom all expenses of such sale and the amount which would be required to pay in full all creditors whose claims are prior in lien or superior in equity to the claims of such nonassenting creditors or the rights of such nonassenting stockholders.

The article further provides that upon any such sale the property may be purchased for the benefit of the new company by the reorganization committee, and in that event there should be applied on account of the purchase price therefor the distributive share of the proceeds of sale of all securities the holders of which shall have assented to the plan and the securities, though not assenting to the plan, of all classes of which two-thirds or more in amount have assented to the plan. The provision for the sale of the properties was inserted because of doubt that the confirmation of a plan, without acceptance by two-thirds in amount of each class of creditors and stockholders, would be within the scope of the bankruptcy power or would be permissible [fol. 568] under the due process clause of the Constitution. Counsel assert that the provision of section 77(b)(5), permitting a sale of not less than a fair upset price, was designed for the identical purpose here in view, that the common stockholders will be given an opportunity to choose between the warrants for class-B common stock and the proceeds available to them from a sale, and that the plan offers them fair and equitable treatment.

The committee's plan, as well as the debtor's plan, is unacceptable to the trustee of the refunding and improvement mortgage, who undertakes to show that the rights of the bondholders are not adequately recognized under either plan. The trustee of the D. & R. G. first consolidated mortgage prefers the committee plan but complains of the diversion of traffic and earnings to the cut-off route reflected in the results. The trustee of the Denver's general mortgage objects to both plans, indicating certain modifications which it considers should be made for the proper protection of the rights of the bondholders. The successor trustee under the R. G. Western first consolidated mortgage prefers the committee plan but contends that the holders of bonds issued under this mortgage are entitled to better treatment than is offered under either plan. The Untermyer family group, owners of D. & R. G. first consolidated mortgage bonds, refunding and improvement mortgage bonds, general mortgage bonds, and prefered stock of the Denver, contend that both plans are unfair to the present security holders in many respects and should be disregarded by the Commission in formulating a new plan. The Security Research Bureau recommends several modifications in the committee plan.

[fol. 569] CONCLUSIONS

The obligations and capital stock of the Denver and its affiliated companies, outstanding on June 30, 1938, were substantially as follows:

	Principal amount	Accrued interest	Total
Equipment obligations	$2,795,000		$2,795,000
Trustees certificates	5,000,000		5,000,000
Junction first-mortg. 5% bonds	2,000,000	$308,333	2,308,333
R. G. Western first-trust 4% bonds	15,190,000	2,126,600	17,316,600
R. G. Western consol. 4% bonds	15,080,000	2,262,000	17,342,000
D. & R. G. consol. 4% bonds	34,125,000	5,460,000	39,585,000
D. & R. G. consol. 4½% bonds	6,382,000	1,148,760	7,530,760
D. & R. G. W. ref. & imp. 5% bonds	12,000,000	2,250,000	14,250,000
D. & R. G. W. ref. & imp. 6% bonds	2,000,000	450,000	2,450,000
D. & R. G. W. general mort. 5% bonds	29,808,000	7,327,800	37,135,800
Notes to Finance Corp.	10,691,850	1,267,619	11,959,469
Note to R. R. Credit Corp.	278,000		278,000
Note to Chase National Bank	1,500,000	206,448	1,706,448
Total secured debt of the Denver	136,849,850	22,807,560	159,657,410
D. & S. L. first-mort. 4% bonds	1,500,000		1,500,000
D. & S. L. income-mort. 6% bonds	9,734,000		9,734,000
Total secured debt of the system	148,083,850	22,807,560	170,891,410
D. & R. G. W. preferred stock, $100 par value*			16,445,600
D. & R. G. W. common stock no par value		(shares)	300,000
D. & S. L. common stock, no par value		(shares)	460

* Accumulated dividends $14,225,444.

The approved plan should provide for the above stated amounts of obligations outstanding, which exclude intercompany holdings and securities under pledge. The amounts of equipment obligations, trustees' certificates, and short-term loans shown are subject to any adjustments [fol. 570] which may be necessary in order to restate the exact amounts of these obligations as of June 30, 1938.

The total debt is nearly $14,000,000 in excess of that outstanding on January 1, 1937, the date when the filed plans were to become effective. Under the provisions of section 77(d) the Commission may, after public hearing, approve a plan which may be different from any which has been proposed, and will, in the opinion of the Commission, meet with the requirements of sub-sections (b) and (c), and be compatible with the public interest.

The consolidation of the several companies for unified operation and management, which is an essential part of the plans that have been presented, is in accord with the Commission's findings in *Consolidation of Railroads*, 159

I. C. C. 521, wherein the Denver and the Salt Lake were grouped in System No. 18—Missouri Pacific. The Western Pacific was also included in that system. The present record is inadequate for a determination of the question of merging the Western Pacific with the reorganized Denver. It justifies the conclusion, however, that the consolidation of the Denver, the Salt Lake Western, the Salt Lake, the Junction, and the Goshen Valley would be in the public interest. Notwithstanding the fact that the Salt Lake, the Junction, and the Goshen Valley are not in trusteeship, and that none of the corporations has sought consolidation under section 5(4) of the Interstate Commerce Act, as amended, as a practical matter, in this case, the Commission may include the proposed consolidation in its plan.

Any corporate action by the existing companies which may be necessary under the requirements of section 5(4) of the Interstate Commerce Act, as amended, will be assured if and when the Commission's plan shall be [fol. 571] accepted in the manner provided in section 77(e). As pledgee of the capital stock of the Salt Lake, the Salt Lake Western, and the Goshen Valley, the Finance Corporation is at present in a position of control with respect to the action of those corporations. The Governors of the States in which the several carriers operate were served, prior to the hearing, with copies of the plan of reorganization filed by the debtor, and advised of the provisions for consolidation contained therein.

Capital Structure Recommended

Hereinafter, the term "new company" will be understood to mean either the reorganized debtor or a new company created to take over the properties of the several existing companies. The new company should assume the equipment obligations outstanding, together with all obligations with respect to claims entitled to priority over the mortgage bonds of the debtor and not paid prior to the effective date of the plan. Unsecured claims, other than those which, by order of the court are to be paid in cash, should be settled on the basis of one share of new common stock for each $100 of claim.

The capitalization of the new company, excluding securities to be pledged, should consist substantially of $2,795,000 of equipment obligations taken over, $51,629,377 of new

first-mortgage 4-percent bonds, $27,453,104 of income-mortgage 4½-percent bonds, $32,541,204, par value, of 5-percent preferred stock, and 371,761 shares of common stock, of no-par-value. In addition, the new company may issue secured notes to the Railroad Credit Corporation and to the Chase National Bank, as of June 30, 1938, representing extensions of the present obligations of approximately $278,000 and $1,706,448, respectively, in the manner hereinafter described. On this basis, the total debt of the new [fol. 572] company would approximate $83,861,929, and the total capitalization, taking the no-par common stock at $100 a share, would approximate $153,579,233. Fixed interest charges would be approximately $2,276,699, contingent interest charges $1,235,390, and preferred stock dividend requirements $1,627,060 per annum. Including the maximum payment of $600,000 to the capital fund and $137,625 to the sinking fund, herein recommended, the proposed annual charges, ahead of dividends on the new common stock, would be about $5,876,414.

Under the committee's plan the total fixed charges would be about $3,032,000 and under the debtor's plan $2,924,000, in both cases based on the obligations outstanding January 1, 1937, except that the equipment obligations outstanding on June 30, 1938, have been included.

Adverting to the evidence pertaining to earning power, hereinbefore summarized under "Traffic; earnings," the actual income of the system lines, available for interest, during the depression years, 1932-35, after intercompany eliminations, averaged $3,606,920 a year. Applying a coverage factor of 1.3 to this sum, the committee tentatively arrived at $2,774,554 as the permissible amount of new fixed interest charges. The actual average income for the period 1934-36 was $3,118,197. As determined by the Commission's Bureau of Accounts, but eliminating the retroactive application of the social security and railroad retirement taxes, the carriers' available income from 1930 to 1934, inclusive, averaged $4,569,235 a year. The foregoing figures are unadjusted for the reduced maintenance charges which obtained during several years. The available income computed by the debtor for the so-called test-period year was $3,926,223, reflecting the result of operating the cut-off during its first year. The ultimate effect on earnings from [fol. 573] the opening of the cut-off route is plainly uncer-

tain. In view of all the circumstances, the fixed charges of the new company should be within conservative limits.

Division 4 should find, from a consideration of the prospective earning power of the system and in the light of the foregoing statement, that there will be adequate coverage of the fixed charges of the new company, as herein proposed, by the probable earnings available for the payment thereof.

The pledging of the 100,000 shares of Utah Fuel Company stock with the trustee of the R. G. W. consolidated mortgage was described in the report of division 4 in *Denver & Rio Grande Western Reorganization*, 82 I. C. C. 745 (753) and in the report of the Commission in the same proceeding, 90 I. C. C. 141 (148). In its brief filed in the present proceeding, the trustee of the mortgage discusses the status of this stock in detail, refers to the report of the mining expert whom it had employed to examine the property and estimate its value, and objects to the value assigned to the stock by the debtor on an earnings basis in providing for the R. G. Western consolidated mortgage bonds. It objects also to the capitalizable value assigned to this stock by the committee. The plans, however, do attempt to recognize a value for the stock through their formula calculations for the R. G. Western consolidated mortgage bonds. As to the disposition to be made of the stock, the debtor would place it under the direct lien of the new general income mortgage, subject to existing rights of redemption for such stock, while the committee proposes to place it under that of the new first mortgage. The former course seems preferable in view of the allocation of new income mortgage bonds to the holders of the R. G. Western consolidated bonds, D. & R. G. consolidated mortgage bonds, [fol. 574] and refunding and improvements mortgage bonds, as herein proposed.

Description of New Securities

The new first mortgage should constitute a first lien, subject only to purchase money liens, including equipment trusts, on all property owned by the companies embraced in the plan or now in the hands of the trustees of the debtor, except the debtor's narrow-gage lines and their equipment, and the stock of the Utah Fuel Company, and on all property acquired by the new company after the effective date

of the plan, subject to purchase money liens. The mortgage should provide for the issue of series-A 4-percent bonds, having a term of 50 years, in the principal amount of approximately $51,629,377 in connection with the reorganization, and additional bonds of other series, with terms not less than 50 years and rates of interest not more than 5 percent per annum, in unlimited amount, provided such additional bonds be issuable only against 75 percent of the capital cost of additions and betterments to roadway, and acquisitions of fixed property, after appropriate deduction for property retired, for the purchase of new equipment free from any other lien, for the refunding of debt, or on the basis of deposited cash. The bonds of series A should be redeemable, in whole or in part, at any time upon 30 days notice, at their principal amount and accrued interest; bonds of later series at premium rates to be determined by the reorganization committee and approved by the Commission with due regard to the dates of redemption fixed for such bonds. (The appointment and duties of the reorganization committee will be described later.) The plan should provide that additional first-mortgage bonds may not be issued on the basis of additions and betterments, [fol. 575] new property, or cash deposited, unless the income available for fixed charges during a period of 12 consecutive calendar months within the 15 calendar months preceding the date of authentication and delivery exceeds 1½ times fixed charges.

The new income mortgage should constitute a lien on the consolidated properties, subject only to the lien of the first mortgage and any liens that may be prior to the lien of the first mortgage, should be further secured by pledge of the capital stock of the Utah Fuel Company, and should be closed at the principal amount of bonds issued in the reorganization, approximately $28,328,000, including bonds to be pledged. The bonds issued under this mortgage should have a term of 75 years, should bear interest at the rate of 4½ percent per annum, cumulative up to a total of 22½ percent of their principal amount, whether such total percent represents interest for consecutive or nonconsecutive calendar years, and should be redeemable, in whole or in part, on any interest date at their principal amount plus accumulated unpaid interest. Provision should be made for a sinking fund for the purchase and retirement of the income mortgage bonds, the payments into such

fund to be made from available net income, as hereinafter provided, at the rate of one-half of 1 percent per annum of the aggregate principal amount of bonds issued in the reorganization.. The income mortgage should provide that the new company shall not create any mortgage lien upon any of its properties other than the new first mortgage, the new income mortgage, and purchase money liens, including equipment obligations.

Each of the new mortgages should provide for the modification or alteration thereof, and of any supplements thereto, and of the obligations of the new company or bondholders thereunder, by concurrent action by the new [fol. 576] company and of the holders of not less than two thirds in aggregate principal amount of the bonds outstanding, provided that such change or modification shall not impair the obligation of the new company to pay the principal or interest of any bond at the time and place prescribed or shall not permit the creation of any mortgage or lien ranking prior to or *pari passu* with the lien of the first mortgage or the income mortgage, respectively, unless the creation of such mortgage or lien be consented to by the holders of all the first-mortgage bonds or income-mortgage bonds, as the case may be.

The preferred stock of the new company should be authorized in the total amount of 500,000 shares, of the par value of $100 each, of which amount approximately 349,396 shares would be issued in the reorganization, including shares to be pledged. Such stock should be entitled to dividends at the rate of 5 percent per annum before any dividends on the common stock are paid or declared. Dividends, as declared by the board of directors, should be paid annually and should be cumulative to the extent earned in any preceding income period, but not paid. In determining the extent earned, deductions for fixed charges, capital fund, contingent interest, and sinking-fund payments should be made as hereinafter provided, and the payments into the funds should not be treated as borrowings from the net income which would otherwise be payable in dividends on the preferred stock, i. e., added back in computing accumulated dividends, as the committee suggests with respect to the capital fund. In a liquidation of the new company, the preferred stock should be entitled to receive its par value, plus unpaid cumulative dividends, before any dis-

tribution shall be made to the common stock. The preferred [fol. 577] stock should be redeemable, in whole or in part, at any time at its par value plus unpaid cumulative dividends.

The committee's plan prohibits certain acts by the new company without the consent of the holders of at least two-thirds in par value of the proposed series-A preferred stock and in number of shares, of the proposed class-A common stock. Such acts include the creation of additional mortgages, the assumption of indebtedness maturing more than two years from its date, the acquisition of property if exceeding $5,000,000, and various other matters. These are the matters primarily within the sphere of the new management, and any action in these respects is subject to approval by the Commission before being put into effect. It is unnecessary, therefore, to specify in the plan all the conditions mentioned. The suggestion for a two-thirds vote of the stock, however, requires consideration. In view of the difficulty of obtaining the vote of so large a proportion of the stock, it is recommended that the charter or by-laws of the new company provide for a majority vote of each class of stock outstanding for the ratification of any assumption of obligations, issue of securities, acquisition of property, execution of leases, making of loans, etc., with respect to which the approval of the Commission is required under any Federal statute.

The committee's plan provides that the new series-A preferred stock shall be convertible into class-A common stock on a share-for-share basis, and that, when the amount of the preferred shall have been reduced to $10,000,000, or less, the holders thereof shall relinquish their rights in the matter of election of directors. This proposal was made in order to facilitate the retirement of the preferred stock, and as "an inflation hedge". While the conditions under which it would be to the advantage of the preferred stock- [fol. 578] holder to convert his holdings into common stock are rather remote, the provision for conversion is in the direction of an improved capital structure and should be incorporated in the approved plan. It will be unnecessary to make any special provision regarding voting rights in this connection under the plan herein recommended.

The common stock of the new company should be authorized in the amount of 500,000 shares, of no-par-value,

of which approximately 406,613 shares should be issuable in the reorganization, including shares to be pledged.

The preferred and common stock should have equal voting rights, each share being entitled to one vote for the election of directors and in all matters of proprietary interest.

Available Net Income; Capital Fund; Sinking Fund

The available net income of the new company should be determined for the 6-months' period ending December 31, 1938, as though the company had come into possession and operation of the properties and had issued the new securities on June 30, 1938, and thereafter for each calendar year ending December 31. The available net income for any income period should represent the income remaining after deducting all fixed charges during that period, together with an amount representing any deficit in fixed charges which may have accrued in previous periods. The available net income so determined should be applied to the following purposes, to the extent that it is sufficient therefor, in the following order:

1. To the payment into a capital fund, on or prior to April 1 of each year, beginning April 1, 1939, of an amount up to but not exceeding 3 percent of the total operating revenues of the system during the preceding income period, [fol. 579] subject to a maximum limit of $300,000 for the initial payment and $600,000 for each succeeding annual payment. Any amount by which the sum available for the capital fund in any year shall be less than 3 percent of total revenues, should not become cumulative against the available net income of the next succeeding income period. In the event the reorganized company shall establish an operating account for depreciation of roadway and structures, payments into the capital fund should be made from the depreciation reserve so created to the extent that it is sufficient.

2. Any available net income remaining after the payment into the capital fund should be applied, on April 1 of each year, to the payment of accumulated interest, if any, due on the income mortgage bonds, limited to a maximum accumulation of 23½ percent of the aggregate principal amount of bonds at any time outstanding, such payments being made in the order of the due dates of such interest.

3. Any then remaining available net income should be applied, on April 1 of each year, beginning April 1, 1939, to the payment of the interest on the income mortgage bonds then outstanding, in even multiples of one-fourth of 1 percent, up to the total rate of 4½ percent per annum, applicable to the preceding income period.

4. Any then remaining available net income should be applied, on April 1 of each year, beginning April 1, 1939, to a sinking fund for the retirement of the income mortgage bonds issued in the reorganization, the payments to be in amounts up to but not exceeding one-half of 1 percent of the aggregate principal amount of bonds outstanding, and to be noncumulative.

5. Any then remaining available net income should be applied, as may be declared by the board of directors, to the [fol. 580] payment of dividends in the order of their priority, or to other proper corporate purposes.

The use of 6-months' income periods for the determination of available net income, and the payment of interest and preferred stock dividends semi-annually, as proposed by the committee, involves successive adjustments of bond interest and the use of interim dividends on the preferred stock in order that the aggregate payments to the security holders shall be based on the earnings of complete calendar years. This method, it is true, would result in a return to the security holders twice a year (earnings permitting), but it is desirable that the result of a full year's operation be ascertained before any contingent interest or dividends be paid (subject to the condition that the initial income period will be six months), and that the entire amount of such interest and dividends earned be paid as soon after the close of the 1-year income period as is practicable. The date of payment suggested above is April 1 in each year.

The limiting amount of the capital fund herein provided conforms to the total annual payments proposed by the debtor for its additions and betterments fund. An adequate reason for changing the amount is not clear from the record. No specific objection to a provision for a capital fund was presented. The new first mortgage and income mortgage should make such provision and should also provide for the determination and application of available net income, as indicated above. The capital fund should be placed in the hands of the trustee under the new first mortgage and

should be withdrawable by the new company to reimburse it for, or to provide for, the cash cost of additions and betterments to the mortgaged property, including equipment, [fol. 581] not previously certified or thereafter to be certified, as a basis for the issue of new first-mortgage bonds, or the release of mortgaged property, or the withdrawal of cash held by such trustee, and further provided that no expenditures so used as a basis for withdrawal of money from the capital fund shall be made the basis for the issue of any securities ranking prior to or on a parity with the new preferred stock. Withdrawals from the fund should be allowable also for the cash payments in connection with new equipment trusts to the extent that the charges to depreciation of equipment in any income period are less than the total cost of the new equipment acquired. The capital fund should be used primarily for additions and betterments to roadway and structures, and the acquisition of new equipment in connection with equipment trusts or otherwise is intended to be provided for by the charges to depreciation of equipment. A sinking fund should be provided for the retirement of first-mortgage bonds, if any be issued for the acquisition of new equipment, free of other liens, by the payment, annually to the trustee, of an amount equal to the quotient found by dividing the principal amount of such bonds by twice the number of years embraced in the effective service life of the equipment. Any money not withdrawn from the fund would be accumulated by the trustee until the amount of the accumulation shall equal the interest requirements of the new first-mortgage bonds for a period of one year, after which the reserve fund would be withdrawable by the new company for the payment of interest on its first mortgage bonds outstanding in any year when its earnings are insufficient for such payment, and only to the extent of such insufficiency.

[fol. 582] *Means of Future Financing*

In the debtor's plan, the means of future financing by the new company, with respect to requirements not covered by the additions and betterments fund and equipment-trust obligations, are provided through bonds to be issued under any of the proposed mortgages, as well as through the new preferred stock. Counsel for the committee take the position that first-mortgage bonds offer the lowest yield and

provide the cheapest form of financing; that the preservation of a sound capital structure will be insured if the new mortgage imposes proper limitations as to the purposes and amounts of additional issues; that fixed interest bonds issued under such conditions and the limitations prescribed in section 77 provide a continuing medium for investment in railroad securities by trust funds and trust institutions, and thus broaden the market for cheap credit. Counsel further contend that there is no necessity for a sinking fund for the retirement of bonds issued under an open first mortgage, such as is contemplated, and that any reduction in the amount of bonds issuable in order to provide for a sinking fund would be unjustifiable, "since it would require the bondholders to pay off their own debts for the benefit of the equity". In the case of income mortgage bonds, which are issued to present bondholders having a vested contract right to the payment of both principal and interest, creditors receiving such bonds are entitled, in the opinion of counsel, to the payment of the principal as soon as it may be done without prejudice to the property. Accordingly, a sinking fund for the retirement of income bonds, issued under a closed mortgage, is considered desirable, provided the payments thereto are made after payments to the capital fund and payments of contingent interest. To the foregoing considerations may be added the uncertain market- [fol. 583] ability of the new company's income bonds. At times of earnings below the level of the contingent interest requirements, such bonds are not likely to be salable on satisfactory terms. The main reason for their issue is that they tend to avert another bankruptcy. They give the security holder no right of foreclosure except upon default on the principal. With respect to the distribution of earnings they are in no better position than a preferred stock, and are in a worse position because they do not give their owners a voice in the management. If the circumstances require that bonds of this character be issued, as is the case here, it seems evident that the mortgage should be closed, and that provision should be made for a sinking fund. The Commission should approve the plan herein described, by which the means of future financing are provided in the new first-mortgage bonds and the new capital stock, and the only sinking fund is that for the retirement of the income mortgage bonds.

Mortgages on the Western Lines

Because of the showing that the earnings of the Denver's Western lines during the test-period year were more than adequate to cover interest charges on the bonds representing first liens on such lines, the debtor proposes that the Junction first 5's and the R. G. Western first-trust 4's be exchanged, in each case, for like principal amounts of new 3½-percent bonds issued under a mortgage secured by a first lien on the Junction property, the R. G. Western property, and the Denver's property lying between Dotsero and Rifle, and between Grand Junction and Crevasse, Colo., thus placing all lines west of Dotsero under the direct lien of the new Western division mortgage. An additional amount of new 3½ percent bonds, or a corresponding pay-[fol. 584] ment in cash, is offered to compensate the bondholders for the loss of interest to maturity on the present Junction bonds and R. G. Western bonds. Such maturities are December 1 and July 1, respectively, 1939. It is contended by counsel for the debtor that the holders of the bonds in question should get all that they could receive in a liquidation or foreclosure. The relatively high earning power of these lines, even on the basis of the cut-off mileage used in the committee's formula, is uncontroverted.

The committee considers that "nothing can duly recognize the position of these bonds short of a new first-lien bond for the total of their principal and accrued unpaid interest, the new bonds to be of such interest rate, maturity, and terms as to sell at par." In order to meet this requirement, as has already been stated, the committee proposes the issue of new series-A bonds having a relatively short term, a permissible interest rate up to 4½ percent per annum, and other features intended to assure the required market value. The committee considers it unnecessary to create a separate mortgage for the Western district.

Since the means of financing a cash payment of the present bonds are not available, a refunding operation, as is proposed by the debtor and the committee, is evidently necessary and proper. But the necessity for the creation of a separate new mortgage on the Western lines, or a separate series of new system bonds, is not entirely clear. Certainly the present bondholders are entitled to a better interest rate than 3½ percent on the new bonds offered them

under the debtor's plan. Under present conditions, however, they cannot reasonably expect to refund on a more favorable basis than 4 percent. The Western division bonds proposed by the debtor would not have a status prior to that of the other new first-mortgage bonds with respect [fol. 585] to the payment of interest. With respect to their lien position, based on the cost of reproduction of the mortgaged lines, less depreciation, it has not been shown that the value supporting each new Western division bond would be in excess of that behind a new first-mortgage bond secured by a lien on the lines of the system. As to the special class of new first-mortgage series-A bonds proposed by the committee, there is not sufficient assurance of their marketability to justify this separate issue, which might result in a considerable increase in the fixed charges of the new company due to the interest rate of 4½ percent allowable under this proposal.

Under the plan herein recommended, the Junction 5's and the R. G. Western first 4's may be exchanged for new first-mortgage 4-percent system bonds in amounts equal to the principal of the present bonds plus unpaid interest. The 4-percent interest rate will do full justice under present financial conditions. Equal justice with respect to the lien will be afforded, as is indicated by the fact, derived from the record, that the cost of reproduction of the Junction property, less depreciation, plus the value of lands and rights, corresponds to approximately $1,732 for each $1,000 of present bonds outstanding, while the cost, less depreciation, of the lines of the system corresponds to approximately $2,820 for each $1,000 of proposed first-mortgage bonds. On the same basis, each $1,000 first-trust bond of the R. G. Western represents a reproduction cost value of approximately $1,809, as compared with $2,820 for the new bond to be offered. Considering the matter in another aspect, the lines of the Junction and the R. G. Western are at present bonded, under first mortgages, at the rates of about $32,300 a mile and $36,600 a mile, respectively, while [fol. 586] the proposed system will be bonded at the rate of less than $20,000 a mile.

Finance Corporation Claims

On the basis of the collateral held by the Finance Corporation as security for its loans to the debtor, and the evi-

dence pertaining to the value of such collateral from earnings and otherwise, the claims of the Finance Corporation are clearly entitled to settlement in full, within the limits of the permissible capitalization. It is unnecessary to describe the evidence in this connection, which is voluminous and conclusive.

Equity in Present Stock; Future Control

Referring to the balance sheet of December 31, 1936, which is the latest one contained in the record, the capital liabilities of the Denver, other than capital stock, together with total current liabilities, deferred liabilities, tax liability, and other unadjusted credits, amount to $154,552,730. Deducting all book assets, other than those representing investments, the net amount was $140,560,266. For the combined properties, after intercompany eliminations, the corresponding figure was $153,314,502, which represents the net debt of the system on the basis of the consolidated balance sheet. Disregarding the balance sheet basis, the total debt outstanding as of December 31, 1936, consisting of equipment-trust obligations, trustees' certificates, loans, and the principal amount of bonds, with unpaid interest, was $157,056,723. According to the debtor's testimony, the capitalizable assets of the system approximate $243,000,000 (including the increase in investment in 1936), but such amount far exceeds any probable value of the physical properties and is unsupported by any evidence as to earning power.

[fol. 587] Both the debtor and the committee object to the use of the valuation data introduced, and the committee doubts that the law of the land requires that any consideration be given to physical values in determining the issues presented. The elements of rate-making value reported to the Commission, however, are pertinent in this connection, and consideration should be given to the finding, hereinbefore recommended, with respect to the cost of reproduction of the system property, less depreciation, plus lands and rights, working capital, and net additions and betterments during 1936. With respect to earning power, in no year since 1930 was the combined net income available for the payment of interest sufficient to cover the charges on the debt outstanding on December 31, 1936, nor, of

course, on the greatly increased debt outstanding on June 30, 1938. In no year has the present Denver company paid a dividend on either class of stock. The average system income available during the 4-year period 1932-35, after intercompany eliminations, if capitalized at 4½ percent, would amount to $80,154,000; the average for the period 1934-36, in large part reflecting the operation of the cutoff, would amount to $69,293,000. The earnings calculated by the debtor to represent the test-period, similarly capitalized, would amount to $87,250,000, and those estimated for a future normal year would represent a capitalization of approximately $138,120,000.

Between December 31, 1936, and June 30, 1938, the total debt of the system, including unpaid interest, increased from $157,056,723 to about $170,900,000, or by about $13,843,000. To that extent any equity for the Denver's present stock has become more remote.

The debtor contends that a substantial equity is represented by its stock, arguing that the bankruptcy of the road [fol. 588] was a temporary condition due to the heavy capital investment in the Dotsero cutoff. The committee, on the other hand, takes the position that there is no equity in either class of stock and that the plan cannot fairly allocate any securities outright to the present stockholders.

The Commission should find that the equity of the holders of the debtor's common stock and of the holders of its preferred stock has no value and that the holders of claims in classes 1 and 2 are, therefore, not entitled to participate in the plan.

Both the debtor and the committee propose that certain considerations be given for the acquisition of stock control of the new company by the present proprietary companies, as has been described. It may be urged that the proprietary companies have valid rights in the premises, that the public interest supports the proposal, and that the consideration passing may be adequate to overcome any question of prior rights. If the Commission shall find, however, that the present stockholders have no equity and are not entitled to participate in the plan, and the new voting stock should be distributed to the present bondholders under some equitable plan, it is not the function of the Commission to make any other provision for the future control of the system. That matter should rest with the new own-

ers, who, in an appropriate later proceeding, may present their proposal to the Commission for its consideration, in the event it is desired that the present interests or others shall exercise control of the new company.

Proposed Allocation of Securities

Conforming to the new capital structure recommended, the assignment of new securities would be as shown in the following table.

[fol. 589]

	Present (June 30, 1938)	Proposed new securities: First-mort. 4% bonds, series A	Inc. mort. 4½% bonds	Pref. 5% stock $100 par value	Common no par value (shares)
Equipment obligations[1]	$2,795,000				
R. R. Credit Corp. loan[2]	278,000				
Chase Bank loan[2]	1,706,448				
Trustees' certificates	5,000,000				
Reorganization exp., etc.	1,009,000	$6,000,000			
Junction first 5's	2,308,333	2,308,333			
R. G. Western first 4's	17,316,600	17,316,600			
		(15%)	(40%)	(45%)	
R. G. Western consol. 4's	17,342,000	2,601,300	$6,936,800	$7,803,900	
			(40%)	(40%)	(20%)
D. & R. G. consol. 4's	39,585,000		15,834,000	15,834,000	79,170
			(40%)	(40%)	(20%)
D. & R. G. consol. 4½'s	7,530,760		3,012,304	3,012,304	15,062
			(10%)	(35%)	(55%)
D. & R. G. W. ref. & imp. 5's	14,250,000		1,425,000	4,987,500	78,375
			(10%)	(35%)	(55%)
D. & R. G. W. ref. & imp. 6's	2,450,000		245,000	857,500	13,475
					(50%)
D. & R. G. W. general 5's	37,135,800				185,679
R. F. C. notes	11,959,469	11,959,469			
D. & R. G. W. pref. stock	16,445,600				
D. & R. G. W. common stock (shares)	300,000				
D. & S. L. bonds	11,234,000	11,443,675			
D. & S. L. stock (shares)	460			46,000	
Totals		$51,629,377	$27,453,104	$32,541,204	371,761

[1] To remain undisturbed.

[2] To be extended.

[fol. 590] The holder of each $1000 Junction first-mortgage bond should receive approximately $1,154, principal amount, of new first-mortgage series-A bonds, representing 100 percent of the principal of such bond, plus unpaid interest, together with a cash payment of $10, representing one year's interest on such bond at 1 percent.

The holder of each $1000 R. G Western first-trust bond should receive approximately $1,140, principal amount, of new first-mortgage, series-A bonds, representing 100 percent of the principal of such bond, plus unpaid interest.

The holder of each $1000 R. G. Western consolidated mortgage bond should receive approximately $172.50, principal amount, of new first-mortgage bonds, $460, principal amount, of new income mortgage bonds, and $517.50, par value, of new preferred stock, such amounts representing 15 percent, 40 percent, and 45 percent, respectively, of the principal of such bond, plus unpaid interest.

The holder of each $1000 D. & R. G. consolidated mortgage 4-percent bond should receive approximately $464, principal amount, of new income mortgage bonds, $464 par value, of new preferred stock, and 2⅓ shares of new common stock, such amounts (taking the common stock at $100 a share) representing 40 percent, 40 percent, and 20 percent, respectively of the principal of such bond, plus unpaid interest.

The holder of each $1000 D. & R. G., consolidated mortgage 4½-percent bond should receive approximately $472, principal amount, of new income mortgage bonds, $472, par value of new preferred stock, and 2⅓ shares of new common stock, representing 40 percent, 40 percent, and 20 percent, respectively, of the principal of such bond, plus unpaid interest.

[fol. 591] The holder of each $1000 Denver refunding and improvement mortgage 5-percent bond should receive approximately $119, principal amount, of new income mortgage bonds, $416, par value, of new preferred stock, and 6½ shares of new common stock, representing 10 percent, 35 percent, and 55 percent, respectively, of the principal of such bond, plus unpaid interest.

The holder of each $1000 Denver refunding and improvement mortgage 6-percent bond should receive approximately $122.50, principal amount, of new income mortgage bonds, $429, par value, of new preferred stock, and 6¾ shares of new common stock, representing 10 percent, 35

percent, and 55 percent, respectively of the principal amount of such bond, plus unpaid interest.

The holder of each $1000 Denver general mortgage bond should receive approximately 6¼ shares of new common stock, representing one-half share for each $100 of principal and interest.

The foregoing amounts of new securities, being mostly in odd figures, due to the accumulations of interest on the present bonds and other circumstances, will require the issue of scrip for sums less than $100, in the case of bonds, and for fractional shares of stock. Provision for the issue of such scrip should be made in the plan.

The holders of the capital stock of the Salt Lake outstanding in the hands of the public should receive, in exchange therefor, an equal number of shares of the preferred stock of the new company. There is no logical ground upon which these stockholders are entitled to mortgage bonds. The system earnings computed by the debtor for the test-period year correspond to approximately $4.21 a share for the Salt Lake stock, but the highest actual earn- [fol. 592] ings of the Salt Lake in any one year since 1929 were only $1.79 a share, and in other years since 1929 they were much less than $1 a share. The equity in the Salt Lake stock on the basis of the cost of reproduction of the property, less depreciation, plus lands and rights, is approximately $62 a share. These facts indicate that an exchange for the preferred stock of the new company would provide amply for the minority stockholders of the Salt Lake. The price which the Denver paid for its acquisition of the majority stock, four or five years ago, is not applicable to the present situation.

The secured note held by the Railroad Credit Corporation should either be paid in cash or extended, at the discretion of the reorganization committee. If the latter plan be adopted, the note of the new company should be in face amount equal to the indebtedness to the Credit Corporation as of June 30, 1938, after any distributive credits which may apply thereon, bearing interest at 4 percent per annum, and payable in six months. The new securities issuable as collateral for such note, representing those for which the present collateral would be exchangeable under this proposed plan, would consist of approximately $264,800 of new income-mortgage bonds, $264,800 of new pre-

ferred stock, and 1,324 shares of new common stock. Upon payment of such note the pledged securities should be canceled.

The secured note held by the Chase National Bank should be canceled and a new note or new notes issued in face amount equal to that of the present note, plus interest accrued to June 30, 1938, such notes to mature in 10 years, and to bear interest semiannually at the rate of 4 percent per annum, contingent upon and limited by the total payment of interest and dividends on the new securities to be pledged. Interest on such note or notes should be cumula- [fol. 593] tive. The new securities issuable as collateral, representing those for which the present collateral would be exchangeable under this proposed plan, would consist of approximately $609,000 of new income mortgage bonds, $2,133,600 of new preferred stock, and 33,528 shares of new common stock. Upon payment of the new note or notes, the pledged securities should be canceled.

The plan should provide for the redemption of all the Salt Lake bonds outstanding, the call price for the first mortgage 4's being 101 and that for the income mortgage 6's being 102. For this purpose, an equivalent amount of new first-mortgage series-A bonds, namely $11,443,675, should be allocated. In order to provide for the payment of the trustees' certificates outstanding, for the expenses of the reorganization, and for working capital, $6,000,000 of new first-mortgage series-A bonds should be issuable in or after reorganization. In respect of the settlement of the claims of the Finance Corporation, there should be allocated approximately $11,959,469 of new first-mortgage series-A bonds, equal to the face amount of the notes outstanding plus accrued interest to June 30, 1938.

The Finance Corporation has indicated that it would accept the committee's plan, which provided for the payment of the debt to that corporation by the issue of certain amounts of new first-mortgage series-B bonds and new income mortgage bonds, and further provided that the Finance Corporation should underwrite the refunding of the Salt Lake bonds. With respect to the $6,000,000 of new first-mortgage, series-B bonds which the committee proposed to make available for the payment of trustee's certificates, reorganization expenses, etc., the plan provided that as many of such bonds as would be required should

[fol. 594] be issued, and sold at such price as might be approved by the Commission.

The financing referred to in the preceding paragraph, involving a total of about $29,400,000, should be arranged, if possible, through private banking channels, the new first-mortgage bonds being sold at or near par. The Commission should require, as part of its plan that, if a commitment on the part of responsible private parties is not obtainable the Finance Corporation will (1) accept the first-mortgage series-A bonds of the reorganized company in full settlement of its claims against the debtor and the secondary debtor, and (2) that it will underwrite the refunding of the two classes of Salt Lake bonds, together with the cash requirement of $6,000,000, on the basis of $17,443,675 of new first-mortgage series-A bonds to be issued for these purposes. The testimony does not indicate that any additional new money will be needed in connection with the reorganization.

General unsecured claims, approved by the court, should be paid in cash or by the issue of common stock, as has been stated. The new company may take any action with respect to the lease or agreement with the Northwestern Terminal Railroad Company as may be lawful under the terms thereof and may adjust, compromise, or settle any claim arising from such action. Except as to this lease, and the agreements, leases, and trackage contracts between the companies to be consolidated, the new company should assume the contracts of such companies which are executory, in whole or in part, and have not been disaffirmed, with the approval of the court, and should also assume any executory contracts made by the trustees of the debtor or secondary debtor, with the approval of the court, which, by their terms, do not terminate at the conclusion of the reorganization proceeding.

[fol. 595] With respect to both the aggregate amount of new securities and the proportionate amounts assigned, the foregoing plan differs materially from the plans presented. It does not represent the application of any one formula but is the result of a review of the entire record.

As a result of a revision of its formula, the debtor materially altered the allocations first proposed, and considered the revision an improvement. The committee's formula as has been explained, constitutes a further revision, based on allowing 42 percent of the constructive

mileage assigned to the cut-off by the debtor, a different conclusion as to the liens of the mortgages with respect to certain equipment and the earnings of the Junction line, and the recognition of accrued fixed-interest charges whether or not earned. In the course of developing these formulas and applying their results concretely, a large number of highly controversial issues were raised at the hearings and were discussed at length in the briefs filed by the parties. The matters in dispute and the contentions made are too numerous to be treated in detail in this report. Several of these matters are legal in character, such as the priority of mortgage liens, and the adjudication of such questions is not properly within the Commission's jurisdiction. However, in view of the departures from the formulas which seem unavoidable these questions are not of great weight. Many other matters open a wide field for judgment and opinion, such as the proper mileage to be allowed to the cut-off, the rental to be charged for use of equipment, the method to be used in computing the profit or loss in operating branch lines, the distribution of terminal expenses, and the basic assumption with respect to earnings which shall represent the relative earning power of each part of the system. As is stated by counsel in the committee's brief, "Obviously, any formula for the segregation of earnings between, and the ascertainment of the relative net income of, various mortgage divisions [fol. 596] offers opportunity for unlimited debate. Many refinements can be requested which may in turn serve as starting points for other inquiries equally protracted".

When an attempt is made to modify either of the formulas by giving effect to the increase in debt since January 1, 1937, and to the capital structure herein specified, the results can by no means be assumed to be those which the debtor or the committee would have reached if they had been governed by the revised data. Under these circumstances, the application of either of the formulas of record would be of doubtful propriety, even if the Commission were in possession of the detailed calculations used in working out these formulas. Consideration has been given, however, to the methods followed and to the assignment of new securities proposed by the debtor and the committee, respectively. It has also been given to the possible effect of distributing the Finance Corporation debt according to the parts of the system for which such debt was incurred.

The distribution of that portion of the test-period income which would remain for the junior bonds, after payments of interest on the prior obligations, has received attention. From all these studies, but without attempting to adjudicate the contested points in detail, the foregoing plan is recommended as meeting the requirement that due recognition shall be afforded to the rights of each class of creditors and stockholders, and that the plan shall not discriminate unfairly in favor of any class.

Miscellaneous Provisions

The debtor proposes that the plan of reorganization, as finally adopted, shall be carried out by it. A board of directors, to consist of 15 members, is contemplated, of which 9 and the president of the new company would be elected by the holders of the common stock.

[fol. 597] The committee suggests a board of 12 directors, of whom 7 would be elected by the holders of class-B common stock. It proposes that the plan shall be carried out by a reorganization committee, consisting of seven members, who would act as voting trustees pending the disposition of the new class-B common stock. All the new common stock, whether of class A or class B, would be issued to the reorganization committee, to be held by it for a period of three years, subject to conditions prescribed.

Since the plan herein recommended provides neither for the issue of stock warrants nor for the vesting of control of the new company otherwise than in the hands of its stockholders, there would seem to be no necessity for the formation of a voting trust. A reorganization committee, to supervise the carrying out of the plan, is desirable owing to the large number of interests and financial operations involved, and the approved plan should provide for such a committee. It should consist of five members, of whom two should be designated by the Insurance Group committee, one by the trustee under the indenture securing the refunding and improvement mortgage bonds, one by the trustee under the indenture securing the general mortgage bonds, and one by the Finance Corporation. The reorganization committee should be authorized to fill vacancies created by death, resignation, or otherwise, preserving the representation of the several interests as before. The committee should determine the method of carrying out the plan,

subject to approval by the court, and the form; and, except as herein otherwise expressly provided, the provisions of all mortgages, bonds, coupons, charter, by-laws, stock certificates, and all other instruments necessary or desirable in carrying out the plan. The number of directors of the new company and the manner of their election should be provided in the new charter or in an amendment of the present charter.

[fol. 598] The plan should be carried out either by vesting the properties of the Denver and its affiliated companies, together with the property held by the trustees, in the reorganized Denver corporation or in a new corporation created for the purpose of this reorganization, and by the execution by the reorganized or new company of the new mortgages and the issue by it of the new securities contemplated under the plan. The effective date of the plan should be June 30, 1938, as of which date the reorganized or new company should be deemed to have come into possession of the properties. The merger or consolidation of the Salt Lake should be effected in a manner to be determined by the reorganization committee, subject to the approval of the Commission and the court.

The provisions of the committee's plan hereinbefore described imposing conditions as to the manner of acceptance of the plan and providing under certain conditions for the sale of the properties at public auction at an upset price should be omitted from the approved plan. Aside from the fact that the statutory majorities required to accept a plan (in the case of creditors, more than two thirds in amount of the total of the allowed claims of the class reported as voting on the plan) are not followed, the proposals may be interpreted as an intended indirect limitation upon the provisions of section 77 permitting the court to confirm a plan, under certain conditions, without a majority of more than two-thirds of each class. The committee's proposal appears to embody a requirement that the two-thirds vote of certain classes shall be a condition precedent to the submission of the plan to the other classes. Insofar as this constitutes an attempted modification of the statutory duty of the Commission to submit an approved plan to all classes, it is objectionable. The committee's proposal makes the sale of the properties at public auction contingent upon whether the plan is accepted by [fols. 599-601] the statutory majority of every class and con-

firmed by the court without the acceptance by all the classes. This is quite different from a direct provision in a plan for a sale at an upset price and the distribution of the proceeds. Furthermore, the proposal described is lacking in essential details as to the securing of funds to effectuate bidding at a public auction of the properties and as to the allocation and issuance of new securities and the payment of claims under the several contingencies of a public sale. For these reasons the proposal is not deemed to provide adequate means for the execution of the plan, and Division 4 should so find. Under these circumstances it is unnecessary for Division 4 to decide whether the provisions of section 77(b) (5) relative to sale of all or any part of the property of a debtor and the distribution of the proceeds derived therefrom could legally be applied to the purposes sought by the committee's proposal.

Division 4 should approve the plan of reorganization and consolidation herein described and should find that such plan will meet with the requirements of section 77(b) and (e) of the Bankruptcy Act, as amended, and be compatible with the public interest; and should render a report and enter an order approving such a plan. Modification of the accounts of the debtor and the other companies involved, as a result of the plan finally adopted, should be subject to the approval of the Commission, and the reorganized or new company should submit its journal entries for such approval before making its permanent accounting records.

In view of the provisions of section 77(f), the Commission, when a plan shall have been finally adopted, should give consideration to the granting of such authority as may be requisite and appropriate for the execution of the plan, including the issue of securities.

Filed Aug. 12, 1938—1:30 P. M. George A. H. Fraser, Clerk.

[fol. 602] IN UNITED STATES DISTRICT COURT

OPINION—December 6, 1940

The Denver and Rio Grande Western Railroad Company, as debtor, and the Denver and Salt Lake Western Railroad Company, as secondary debtor, filed November 1, 1935,

petitions in this court alleging they were unable to pay their debts as they matured, and desired to effect a plan of reorganization under Section 77 of the Act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. On the same day the petitions were filed the court entered orders approving the petitions as properly filed, and authorized and directed the debtor to operate and maintain both properties under the supervision of the court. Copies of the petition and the orders were duly transmitted by the Clerk of this [fol. 603] court to the Interstate Commerce Commission. Orders were made on July 17, 1936, and September 4, 1936, fixing the time within which, and the manner in which, claims and interests of the creditors and stockholders should be filed, and the division of creditors and stockholders into classes for the purpose of the plan and its acceptance.

On November 18, 1935, Wilson McCarthy and Henry Swan were appointed Trustees for the debtor. These appointments were ratified by Division 4 of the Interstate Commerce Commission. On December 19, 1935, the court appointed Raymond L. Sauter Trustee of the secondary debtor, the Denver and Salt Lake Western Railroad Company. This appointment was likewise ratified by the Interstate Commerce Commission. April 29, 1936, upon petition of the debtors, an order was made extending the time for filing a plan of reorganization under Section 77 (d) to and including August 1, 1936. On July 29, 1936, a proposed plan of consolidation and reorganization, as of January 1, 1937, was filed with the court and the Interstate Commerce Commission by the debtor. This plan included the Denver and Rio Grande Western, the Salt Lake Western, the Denver and Salt Lake Railway Company (the Moffat Road), the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company.

In accordance with the procedure prescribed in Section 77, and after due notice, public hearings on the plan began and were held before the Interstate Commerce Commission in October, 1936, and in February, April and June, 1937. On [fol. 604] June 15, 1937, a plan of reorganization, including the companies covered by the debtor's plan, was filed by the so-called "Insurance Group Committee," an intervener, of which George S. Van Schaick was chairman. In addition to this group other interveners included the trustees under certain mortgages, the Security Research Bu-

reau, the Untermyer family, Chase National Bank of New York, the Railroad Credit Corporation, various chambers of commerce and boards of trade, the Reconstruction Finance Corporation and others.

An order of this court of November 23, 1936, divided the claims and interests of the creditors and stockholders into the following classes: class 1, common stock; class 2, preferred stock; class 3, claims entitled to priority under Section 77(n); class 4, claims which would have been entitled to priority over existing mortgages or other liens if a receiver in equity had been appointed for the property; class 5, claims not included in classes 3 and 4, entitled to priority by the laws of any state or the United States; class 6, bonds issued under the Consolidated Mortgage of the Denver and Rio Grande Railroad Company, dated July 15, 1886, and owned by the debtor; class 7, bonds issued under the First Trust Mortgage by the Rio Grande Western Railway Company, dated July 1, 1889, and assumed by the debtor; class 8, bonds issued under the First Consolidated Mortgage of the Rio Grande Western Railway Company of April 1, 1889, and assumed by the debtor; class [fol. 695] 9, bonds issued under the first mortgage of the Rio Grande Junction Railway Company, dated December 1, 1889, assumed by the debtor; class 10, bonds issued under the debtor's Refunding and Improvement Mortgage, dated February 1, 1924, and bonds issued under the Improvement Mortgage of the Denver and Rio Grande Railroad Company, dated June 1, 1888, which may be held to be pledged under the aforesaid Refunding and Improvement Mortgage; class 11, bonds issued under the debtor's General Mortgage, dated February 1, 1924, and bonds issued under the Improvement Mortgage of the Denver and Rio Grande Railroad Company which may be held to be pledged under the aforesaid Refunding and Improvement Mortgage; class 12, secured notes of the debtor held by the Railroad Credit Corporation, the Chase National Bank of the City of New York, and the Reconstruction Finance Corporation, and the debt of the Denver and Salt Lake Western Railroad Company, represented by the debtor's demand note pledged by the Denver and Salt Lake Western Railroad Company as security for a loan from the Reconstruction Finance Corporation; and class 13, all other claims not coming within any of the aforesaid specific classifications.

By report and order of July 11, 1939, the Commission approved a plan of reorganization for the Denver and Rio Grande Western Railroad Company and the Denver and Salt Lake Western Railroad Company, secondary debtor, [fol. 606] The Denver and Salt Lake Railway Company, the Rio Grande Junction Railway Company and the Goshen Valley Railroad Company. Thereafter, on September 1, 1939, petitions for modification of the approved plan were filed by the so-called Insurance Group Committee, by Guy A. Thompson, Trustee of the Missouri Pacific Railroad Company, the Central Hanover Bank and Trust Company, Trustee under the First Trust Mortgage of the Rio Grande Western Railway Company and the First Mortgage of the Rio Grande Junction Railway Company, the United States Trust Company of New York, Trustee under the Consolidated Mortgage of the Denver and Rio Grande Railroad Company, the Guaranty Trust Company of New York, Successor Trustee under the First Consolidated Mortgage of The Rio Grande Western Railway Company, the City Bank Farmers Trust Company, Trustee under the General Mortgage of The Denver and Rio Grande Western Railroad Company, the Moffat Tunnel Improvement District and Moffat Tunnel Commission, and the Security Research Bureau, all interveners herein, and by the debtor and its subsidiaries.

By order of the Commission the parties to the proceeding were permitted to file briefs and reply briefs, and thereafter the Commission, having reconsidered its prior report and order, came to the conclusion that certain provisions of the plan should be modified and certain other provisions, as to which some question had been raised, should be retained without change. And on April 2, 1940, the Commis- [fol. 607] sion entered an order setting forth and approving a modified plan of reorganization for the Denver and Rio Grande Western Railroad Company and the Denver and Salt Lake Western Railroad Company, effective June 30, 1938, and revoking and superseding the order of July 11, 1939.

This order having been certified and filed in the court on April 11, 1940, on May 6, 1940, we ordered all parties in interest to file their objections to the plan of the Commission and their claims, if any, for equitable relief on or before July 1, 1940, and set said objections and claims for equitable

relief for hearing on Monday, July 29, 1940, and providing for time for filing briefs, and that notice of the order should be given to all parties.

In accordance with said order the matter came before this court July 29, 1940, for hearing upon the specific written objections to the plan and claims for equitable treatment (Tit. 11, Sec. 205, subdivision(e), U. S. C. A.). Testimony was taken every day up to August 12, 1940, at the conclusion of which, and before argument, at the suggestion of counsel, an informal conference with counsel was held in the court chambers, and at the request of counsel the court indicated its views as to certain features for a proper plan of reorganization (see interim memorandum of August 30, 1940), stating therein that any plan approved by the court should be within the framework of the Interstate Commerce Commission plan; that it strongly favored the consolidation of the Salt Lake and the Denver—which all the testimony supported—and setting out other requirements [fol. 608] of any plan the court would approve, and emphasizing that the amount of fixed charges in any plan the court would approve was that fixed by the Interstate Commerce Commission, to-wit, $29,403,144.00 of fixed interest first mortgage bonds, total fixed charges $1,278,539.00.

As to the allocation of the first mortgage bonds, the court indicated the three divisional mortgages, i.e., Rio Grande Western First Trust 4s, Rio Grande Junction First 5s and part of the Denver and Rio Grande Consolidated 4s and 4½s, "should share the new fixed interest first mortgage bonds with the Reconstruction Finance Corporation notes on such a proportionate basis as the Rio Grande Junction rate of bonded indebtedness per mile for each of such mileage, thereby awarding new fixed interest first mortgage 4s to these three divisional first mortgages, and to the Reconstruction Finance Corporation notes as follows: Rio Grande Western First Trust 4s, $4,557,000.00, 30%; Rio Grande Junction First 5s, $1,000,000.00, 50%; Denver and Rio Grande Consolidated 4s and 4¼s, $1,012,675.00, 2½%; Reconstruction Finance Corporation notes, $5,389,794.00, 50%."

This allocation of first mortgage bonds, differing from the Interstate Commerce Commission plan, was based on traffic density between Dotsero and Salt Lake City. It is, however, recognized that the Rio Grande Junction 5s, for instance, cover sixty miles of track running from Rifle to

Grand Junction. This particular mileage produces sub-
[fol. 609] stantially no local business. Its earning power is due to its strategic position as a bottle-neck connecting the main line west into Salt Lake with the two eastern lines; Dotsero to Denver and Dotsero to Pueblo, respectively. The system could afford, if necessary, to cut it off, turn it over to its bondholders, and duplicate this mileage with a better and straighter line at a cost of less than $3,000,000.00. In addition, the mileage between Dotsero and Salt Lake City covered by these mortgages is dependent upon the system as a whole for equipment, terminal facilities, shops and overhead organization and personnel.

The court is still of the opinion expressed in the interim memorandum, that the amount of fixed charges of any approved plan should not exceed the interest on the first mortgage bonds in the amount called for by the Interstate Commerce Commission plan. I agree with the views of the Commission as to the probable earnings (printed record Vol. 5, part 4, p. 5104, et seq.).

According to the so-called Eastman Formula said to have been suggested to Congress by Commissioner Eastman, fixed charges under a reorganization plan should not exceed 80% of the net available for interest in the three worst years of the last ten. Applying this to the Rio Grande and the Salt Lake for the ten years 1930 to 1939, we find the worst years were 1938, 1937 and 1934 in the order named. The net available for interest in this period totaled for the three years $7,461,000.00—an average of $2,487,000.00 per
[fol. 610] year. Eighty per cent of this would be $1,989,600.00, without any provision for capital fund, and, of course, the property cannot be operated without some expenditures chargeable to operating expenses. The above figure $7,461,000.00 includes $2,885,035.00 chargeable to operating expenses in connection with improvements. Deducting this, the net available for interest would be reduced to $4,575,965.00, or an average of $1,525,000.00, 80% of which would be $1,220,000.00 as a permissible fixed charge, with no provision for capital fund.

Attention is again called to the fact that the revenue per ton mile for 1939 was $.01018. The corresponding figure for the first eight months of the current year is $.00953, and for the month of September, 1940, $.0088, indicating no improvement in prospective earnings except through increased bridge traffic. In dollars and cents the total esti-

mated operating revenues for the year 1940, up to and including November 14, 1940, are $22,567,580.00—an increase of $865,983.00, or 3.99% over the corresponding period in 1939. This on approximately 255,000 carloads handled to November 23rd this year as compared with 238,000 carloads for the same period in 1939.

Number of carloads handled for the period January 1st to November 14, 1940, was 246,519, as against 230,337 for the same period 1939—an increase of 16,182 cars, or 7.03%, with an increase in dollar revenue of only 4.98%. The increase in bridge traffic for 1939, compared with 1938, shown in the debtor's report to the Interstate Commerce [fol. 611] Commission is:

	Cars	% of Total	Tons	% of Total	Revenue	% of Total
1938	71,084	29 24	1,779 417	22 41	$7,068,516	33 05
1939	81,301	31 34	2,021,174	23 50	8,124,985	35 82

The first six months of 1940 show 38,367 carloads of bridge traffic, compared with 32,794 for 1939—an increase of 5,573 cars, or approximately 17%, with an increase of but 9.59% for all traffic. These figures indicate the increased importance of bridge traffic to this system, and are at the same time primarily responsible for the reduction in net ton mile revenue. This change in traffic from local to bridge is reflected in the average length of haul in September, 1940, of 314.6 miles, compared with 290.9 miles in 1939—an increase of 8.15%.

This large growth of bridge traffic in relation to total tonnage emphasizes the need for continued improvement in track and equipment to enable the debtor to maintain the shorter schedules between the Pacific Coast and Missouri River forced by competitors; for if this property were relegated to its strictly local business, the earnings would not justify fixed charges in any such amount as is contemplated.

The building of this railroad system began in 1871, and a narrow gauge line from Denver to Pueblo was completed in 1872. Thereafter the main line was gradually extended west up the Arkansas River from Pueblo, and reached Leadville in 1880. All of the construction thus far had been narrow gauge, but the threat of competition resulted in a [fol. 612] third rail being laid from Denver to Pueblo, completed in 1881. The property went into receivership July

12, 1884. This receivership was concluded in 1886 when the Denver and Rio Grande Railroad Company acquired the property at foreclosure sale.

In the following year the road was built to Glenwood Springs, Montrose to Ouray, and from Pueblo south to Trinidad and Walsenburg. In 1889, in connection with the Colorado Midland Railroad, it organized the Rio Grande Junction Railway Company, which constructed a line from Rifle Creek to Grand Junction. By the fall of 1890 connection had been made at Grand Junction with the Rio Grande Western, thus forming a standard gauge line from Denver to Ogden, Utah.

In 1905 construction of the Western Pacific line from Salt Lake to the Pacific Coast began to take shape; $50,000,000.00 of construction bonds were sold and work begun. The necessity of this line was the result of the failure of the Central Pacific—owner of a line from Ogden, Utah, to San Francisco—to remain neutral as between the Denver and Rio Grande—then part of the so-called Gould system—and its competitor, the Union Pacific. About that time the Union Pacific interests had acquired control of the Southern Pacific—which in turn owned the capital stock of the Central Pacific. This made it necessary for the Rio Grande system to have its own line from Salt Lake to the Coast. The story is told in the opinion of the Supreme Court in [fol. 613] U. S. v. Union Pacific Railroad, 226 U. S. 61, at pp. 90-91, where the court said that the consolidation of the Union Pacific with the Southern Pacific "practically destroyed the carrying trade from Ogden to the east for the Rio Grande system and necessitated the construction by the latter road of a new connection for California points." The Western Pacific issued its capital stock to the Denver and Rio Grande and the latter guaranteed to pay so much of the interest on the Western Pacific bonds as the Western Pacific net earnings might fail to provide, and also guaranteed the full payment of the principal at maturity.

In March, 1915, the Western Pacific defaulted on its bonds and went into receivership, and suit against the Denver and Rio Grande on its guaranties was instituted in New York by the mortgage trustee. Judgment went against the Denver for $38,000,000.00, and receivership for the Denver and Rio Grande followed. The property was sold at the upset price of $5,000,000.00, and was bid in by Western Pacific interests and reorganized as The Denver and Rio Grande

Western Railroad Company. This receivership ended July 31, 1921. Another receivership followed on August 1, 1922. In the course of this latter proceeding a large rehabilitation program was undertaken under the direction of the court. The main line between Denver and Salt Lake was put in splendid condition, many grades and curves eliminated, new rail laid and ballasted and new power bought. This receivership terminated December 20, 1924, and the existing company, The Denver and Rio Grande Western Railroad [fol. 614] Company, took over the property, and completed and supplemented the improvement program initiated by the court—all at a cost of $40,000,000.00.

Beginning with 1930 operating revenues on the system began to decline, maintenance was largely curtailed, and the property suffered accordingly, so at the start of this Section 77 proceeding it was estimated by disinterested experts that six or seven million dollars was necessary to make up the deferred maintenance and rehabilitate the right-of-way, and $4,000,000.00 for improvements and additions to rolling stock. At the time of the last previous receivership the rail on the main line between Denver and Salt Lake was ninety pounds a section, and the depth of ballast averaged only eight inches on the main line.

In this proceeding the Trustees, under the authority of the court, have laid 242.18 miles of 112 pound rail, 33.47 miles of 131 pound rail, principally on curves, have rebuilt and eliminated many bridges and culverts. In addition five standard gauge passenger locomotives, ten standard gauge freight type locomotives, 1500 steel box cars and 155 cars of various types, such as ballast, tank acid cars, etc., have been purchased. Three hundred stock cars have been built in the company's shops, together with fifteen air-conditioned parlor coaches and seventy-eight automobile cars, and all equipment has been rehabilitated. 255.12 miles of main line has been ballasted. The cost of these improve- [fol. 615] ments, which includes large additions to the shops, yards, tracks and sidings, and improvements of many various kinds, is $23,134,484.00, financed in part by sale of Trustees' Certificates and Equipment Trust Certificates. In addition the operating personnel has undergone a thorough rehabilitation.

One of the outstanding accomplishments of the Trustee management has been the installation of a testing and research laboratory equipped with Magnaflux units and equip-

ment for making photoelastic studies to detect in the laboratory causes of failures due to high stress concentrations, equipment for making photo-micrographs for testing the strength of various materials, and equipment making accelerated tests to determine aging properties, that detect incipient failures in metal equipment, etc. The result is that all materials—including those formerly bought by trade names—are now thoroughly tested before being put in use, and it has been found that car trucks, rails, locomotive rods, pins, rail joint bars and materials of various classifications too numerous to list have in many cases been found defective by laboratory tests. The intangible savings resulting therefrom are impossible to evaluate, because there is no way of ascertaining the damage to property and loss of lives that might have resulted from failure of these materials in use on line. This laboratory has attracted much attention, and other railroads are availing themselves of its services. Cash subsidies are being made to this work by industrial manufacturing companies for research work of benefit to the debtor, as well as the industry generally.

[fol. 616] The net result of the Trustees' operations is that the road today is in the best condition physically it has ever been. Furthermore, as a result of the time and attention directly given to their job by its Trustees, new transcontinental business has been secured, and the standing and reputation of the system among shippers and the public generally whom it serves has been vastly improved. The extensive improvement program referred to has not included every facility necessary to enable it to serve its public and compete successfully. Certain realignments of track, new signalling devices and new passenger equipment similar to that being adopted by railroads throughout the country generally is most necessary, not only to improve service, but to cut the costs of operating, especially on the narrow gauge part of the system. Furthermore, attention in the near future must be given to the question of new power for the operation between Denver and Bond through the Moffat Tunnel, preliminary studies for which are now under way. These factors must be kept in mind in dealing with the question of prospective earnings and possible savings in operation.

The debtor's main line from Denver to Salt Lake via Pueblo and Tennessee Pass is indirect, very long, with

heavy grades. This has prevented it from acting as a bridge carrier of general merchandise from the Pacific Coast to Missouri River points and Chicago. Following a marked decline in local business, such as mining, lumbering, etc., several years ago it became very evident that if the prop- [fol. 617] erty was to exist it must develop overhead or bridge traffic. It was in an attempt to correct this situation the debtor was wrecked financially by its guarantee of the bonds issued to construct the Western Pacific Railroad, with the resulting financial difficulties already enumerated.

The Moffat Road—the Denver and Salt Lake Railroad Company—had been built 232 miles from Denver to Craig, Colorado. The line crossed the Continental Range at James Peak at an elevation of 11,660 feet, which made all year operation practically impossible. To correct this the Moffat Tunnel Improvement District was created in 1922 as a local municipal improvement district to build a tunnel under James Peak to be financed by a property assessment on the entire district, which included the City of Denver and other counties through which the Moffat Road runs. The Tunnel was thereafter built as a local improvement at a cost of approximately $15,000,000.00, for which the District bonded itself.

The Supreme Court of the United States in sustaining the constitutionality of the Moffat Tunnel Act had this to say concerning it as a matter of public policy, Millheim v. The Moffat Tunnel Improvement District, 262 U. S. 710:

> "Furthermore, while the saving of the Moffat road to the people of the State seems to have been the prime motive which induced the passage of the Act, it specifically provides for the use of the tunnel by any and [fol. 618] all railroads and other public utilities to the extent of its capacity, each paying an annual rental apportioned to the respective values of the separate uses, and constituting a fair and just proportion of the total amount required to pay interest on the bonds, provide for their retirement and maintain the tunnel. And the evidence strongly indicates that the tunnel may and will be used, to like advantage by the Denver & Rio Grande Railroad, extending from Denver to Salt Lake City with a great shortening and improvement of its line * * * These are all public purposes of much importance. We conclude that the purpose for which

the tunnel is to be constructed is not private, but public, and as such warrants the exercise by the State of the power of taxation."

At two points on the Colorado River west of the Moffat Tunnel the main lines of the Moffat Road and the Denver and Rio Grande are only thirty-eight or thirty-nine miles apart. In 1928 the Denver and Salt Lake, through its subsidiary, the Denver and Salt Lake Western Railway Company, planned to construct a line of railroad down the river from Orestod on the Moffat line to connect with the Rio Grande at Dotsero. For the purpose of building this so-called cut-off the Denver and Salt Lake Western borrowed $3,631,000.00 from the Reconstruction Finance Corporation. Work was commenced in November, 1932, and the line opened for operation on June 15, 1934.

[fol. 619] About this time the Denver and Rio Grande, having acquired control of the capital stock of the Moffat Road, acquired by agreement trackage rights through the proposed tunnel into Denver, and took over the ownership of the Denver and Salt Lake Western—the connecting link between Dotsero and Orestod—built by the Denver and Salt Lake Western, following permission so to do granted by the Interstate Commerce Commission. This joint trackage agreement provides that the Rio Grande should pay the Moffat Road as rental for use of its line and the Moffat Tunnel $300,000.00 a year, plus one-half of five and one-half per cent per annum for additions and betterments to the property, one-half of the rental of the Moffat Tunnel, and one-half of all betterments and improvements to the Moffat Tunnel, and certain other charges. The Rio Grande also borrowed from the Reconstruction Finance Corporation $3,110,850.00 to enable it to acquire all the rest of the stock of the Salt Lake Railroad Company.

In 1935 the Denver and Rio Grande Western Railroad owned and operated 1628 miles of standard gauge track and 752 miles of narrow gauge track—a total mileage of 2380. By use of the Salt Lake track from Dotsero through the Tunnel to Denver, the debtor shortened its line from Denver to Salt Lake City approximately 175 miles with greatly reduced grades and curvature. At the same time expenses were pared and necessary maintenance greatly curtailed, with the result that its ability to perform its duty as a public utility became greatly impaired.

[fol. 620] The recurrent bankruptcy reorganizations of this property naturally invite an examination of its financial history. It is evident therefrom that the reorganization structures, drawn up by the debtor's bankers and approved by this court in past equity receivership proceedings, have not been able to stand the strain of the excessive fixed interest charges called for and the insistence by bondholders on payment thereof, irrespective of whether earned or not.

The record discloses that previous to the initiation of this particular proceeding the debtor borrowed money from the Reconstruction Finance Corporation, with the consent of the Interstate Commerce Commission, to pay current taxes and interest not earned on underlying mortgage liens—a practice that cannot be defended.

The bulk of long time financing of the major American railroad systems has been largely through the issuance of bonds, to the exclusion of stock. It is recognized more and more by students of such matters that too large a proportion of railway financing should not be in the form of fixed interest bonds, and that investors in the securities of our transportation systems should be considered more as stockholders entitled to dividends out of earnings, rather than creditors legally entitled to demand payment of interest and principal on fixed dates, regardless of whether earned or not.

The history of this property, like that of the many other railroad systems, demonstrates that, as a result of this prac-[fol. 621] tice, during times of depression and bad business the road has found itself unable to meet interest charges or the principal of its debt as it has matured. The bondholders and their trustees have forced foreclosures and receivership proceedings, thus in effect exercising their undoubted right to have the property sold for cash and receive the proceeds up to 100 per cent of their claims. But the net result in each case has been that while the form has been followed the property has not actually been sold for cash, and the bondholders have received no payment on their principal. In each instance they have merely exchanged old securities for new ones in a reorganized company—often forced to take a junior lien. In addition the excessive costs of these court proceedings have been capitalized into new securities and put ahead of the bondholders' claims. The security-holders have thus paid the costs of these receiver-

ships and the rehabilitation of their property while in the hands of the court.

There is much justification, therefore, for the observation by writers on the subject that a fixed interest bond is not really a binding promise to pay the principal and interest of the bond, but contains an implied option in favor of the railroad borrower to pay the bondholder with a junior bond and some stock in place of cash perhaps in a reorganized company. So that a railroad bond therefore becomes merely a claim to a portion of the income and corpus of the property that takes precedence over the claims of other creditors.

[fol. 622] This is the fourth time this property has been in this court for reorganization, the second one under me. The history is always the same, namely, earnings that should properly be expended on maintenance and improvement of the property in order that it may better perform its duty to the public as a carrier of goods and persons for hire has been used to pay interest not earned. Thus the court in each proceeding has found it necessary to, and has, borrowed large sums of money, and has used it to rehabilitate the property, thus in effect restoring and capitalizing ahead of the old existing debts the funds wrongfully diverted under private management. Having in mind the history of this particular property and the failure of the last reorganization, the desire of the court to promulgate a plan of reorganization that will keep the property out of the bankruptcy court in the future and enable it to meet its obligations and perform its duties to the communities it serves should be apparent to everyone.

With a large proportion of the railroad mileage of the country in the hands of federal courts under Section 77, there is strong likelihood that if the many pending reorganizations now before the Interstate Commerce Commission and the courts are not successful, Section 77 will be replaced by a far more drastic procedure with results far less satisfactory to security-holders, who seem loath to recognize and take the loss they have suffered as the result of a short-sighted policy they and their mortgage trustees have been parties to in the past.

[fol. 623] All parties should bear in mind that Section 77 expresses the public policy which led to its enactment, and demands that the operation of railroads be continued for the benefit of the public, regardless of the interests of their

creditors and stockholders. The first objective of a reorganization is to make the railroad a sound, economic unit, able to operate its business successfully and pay a reasonable return to those having an interest in it. Furthermore, any plan approved should aim to cure the financial and business ailments of the debtor, and should not merely provide immediate relief, but be drastic enough to assure continued solvency of the enterprise, even under unfavorable conditions.

On October 31, 1940, a conference was held in my chambers with Eugene A. Schmidt, Jr., and Richard K. Paynter, Jr., of New York City, who had requested permission of the court to present and discuss the so-called Discussion Plan, which represented the consensus of opinion of the parties in interest, tentatively agreed upon at a conference held in Washington, pursuant to the suggestion of the court in its interim opinion, in which the court requested that the parties agree upon a plan for presentation to the court before the next hearing set for October 21, 1940. The court consented to such conference upon the consent in writing of all parties to the record, except the Reconstruction Finance Corporation, which was represented by W. W. Sullivan. The proceedings of said conference are in the record. [fol. 624] At the conclusion, the hearing, which had been postponed until November 13th, was formally set over to January 6, 1941, on the understanding the parties could confer again with the court if they care to.

Consideration having been given to the plans of the debtor, the Insurance Group, the Interstate Commerce Commission and the so-called Discussion Plan, the testimony at the hearing and the record certified by the Commission, the function and duty of the court are no less here than they are in equity receivership reorganization, in respect to which the Supreme Court in Case v. Los Angeles Lumber Co., 308 U. S. 106, at 115, said:

> "'Every important determination by the court in receivership proceedings called for an informed, independent judgment.'"

And, p. 125, Case v. Los Angeles Lumber Co.:

> "Once the property is in the hands of the court private rights as respect that res are subject to the superior

dominion of the court, and are to be adjudicated pursuant to the standards prescribed by the Congress."

And, p. 126 of the same case:

"Furthermore, stockholders and other junior interests may be excluded from any plan of reorganization if the court finds that the debtor is insolvent."

And, p. 114:

"The fact that the vast majority of the security holders [fol. 625] have approved the plan is not the test of whether the plan is a fair and equitable one."

I approve the findings and the plan of the Interstate Commerce Commission certified by its order of April 2, 1940, with certain adjustments within the framework of that plan, which I shall now outline.

These adjustments are occasioned primarily by the proposed sale to the debtor's connecting carriers to the east, to-wit, the Missouri Pacific, connecting at the Pueblo gateway, the Chicago, Burlington & Quincy at Denver, and the Chicago, Rock Island & Pacific at Colorado Springs, half way between Denver and Pueblo, of a new issue of common stock in the reorganized company having sole voting power, for the sum of $10,000,000.00 in cash. This stock should be distributed in the following proportions: Missouri Pacific forty per cent, Burlington forty per cent and the Rock Island twenty per cent, to insure that no one of the three should have control of this voting stock. The receipt of this cash by the reorganized company would reduce to that extent the amount of new fixed interest bonds to be sold under the Interstate Commerce Commission plan for cash to the Reconstruction Finance Corporation, and thus increase the amount of new fixed interest bonds available under the latter plan for distribution to the various divisional mortgages of the debtor (in the proportion outlined in that plan), after making equitable provision for the old loans made by the Reconstruction Finance Corporation to the debtor, with the result that the call upon that corpora- [fol. 626] tion to purchase new bonds for cash will be substantially less than the amount called for by the Interstate Commerce Commission.

If the so-called Discussion Plan represents an effort on the part of certain parties to this proceeding to reach an agreement within the framework of the plan, and within the views of court expressed in the interim memorandum, it succeeds in neither. The order of the Interstate Commerce Commission dated July 11, 1939, Finance Docket No. 11002, Denver and Rio Grande Western Railroad Company Reorganization, reads in part as follows:

> "The grand total of cash thus required will be approximately $17,443,675.00 subject to such change or adjustment as may be found reasonable and proper by the Reorganization Committee and approved by the Court. The Reconstruction Finance Corporation shall file with the Court prior to the referendum on the plan a commitment that it will, upon appropriate authority by this Commission, purchase at par approximately $17,443,675.00 of the new first mortgage series 'A' bonds or such other principal amount thereof as may be needed by the *above mentioned cash financing.*"

The Discussion Plan should be and is rejected, primarily because it fails to provide the necessary new cash required. It merely suggests the willingness on the part of the connecting carriers to purchase for $10,000,000.00 the new [fol. 627] equity stock controlling the management. Granted this commitment is affirmed to the satisfaction of the court, the cash funds necessary to carry out the Interstate Commerce Commission plan would still be short by approximately $7,443,675.00. The Discussion Plan is also rejected because it provides for a relative distribution of the senior securities, to-wit, the first mortgage bonds of the reorganized company, to the various mortgage divisions of the debtor—wholly inconsistent with the distribution provided for in the Interstate Commerce Commission plan. Its proposed treatment of the Rio Grande Western First Trust 4s at 100 per cent and the Denver and Rio Grande Consolidated 4s and 4½s at five per cent is manifestly unjust to the consolidateds.

While a scaling down of all claims must be expected in any reorganization, the Interstate Commerce Commission plan is a little too drastic in asking the Consolidated bondholders to subordinate their prior lien on that part of the line—Pueblo, Dotsero and to the west, which carries the

heaviest traffic—in favor of the issue of the new first mortgage bonds in which they have no participation. Such treatment hardly "affords due recognition to the rights of each class of creditors or stockholders."

Furthermore, we are unable to accept the Discussion Plan for the reason it has no reasonable chance of success. The holders of the Denver and Salt Lake bonds are obviously better off with their present security, income and market value than they would be after the exchange proposed in the [fol. 628] Discussion Plan. These bonds are neither due nor in default as to the payment of principal or interest. Their position is such that they feel it is not necessary for them to be represented before the court in these proceedings.

In our interim memorandum it was indicated the extent to which we thought these Reconstruction Finance Corporation loans had been too favorably treated at the expense of the Divisional First Mortgages, and urged the interested parties to attempt to reach a voluntary agreement among *themselves within* the outlines of the Interstate Commerce Commission plan and the court's views as expressed. For the reasons stated the Discussion Plan does not represent such an agreement, and is neither within the framework of the Commission Plan nor does it comply with the views of the court as expressed.

The Interstate Commerce Commission plan, as I have indicated, gives very favorable treatment to the old advances of the Reconstruction Finance Corporation to the debtor. Nevertheless its collateral, consisting principally of the securities of the Denver gateway, is essential competitively to the future operation, perhaps even to the existence of the reorganized company, and because of the dependence of the success of the plan upon it furnishing the new money necessary to put any plan into effect, it is entitled to preferential treatment.

As observed, the new factor injected into the situation is [fol. 629] a suggestion that the connecting carriers on the east are willing to pay $10,000,000.00 for voting control of the reorganized company. This will correspondingly lighten the burden of the Reconstruction Finance Corporation to furnish new money to carry out the Interstate Commerce Commission plan, and for that reason it is hoped the Reconstruction Finance Corporation, relieved of the necessity of furnishing $10,000,000.00 of new cash, will be content

with somewhat less favorable treatment on its old advances to the debtor corporation.

Another adjustment the court believes proper is the so-called Capital Fund of $750,000.00. This sum, while believed to be inadequate, should be set aside and earmarked as a special cash fund and used only to pay the costs of additions and betterments to plant, properly chargeable to capital account, which have not been previously certified to the Trustee under the new first mortgage as the basis in whole or in part for the issue of additional bonds, and also marked for operating expenses incident to improvements, and may not under any circumstances be used for the payment of dividends or interest on any debts, fixed or contingent. This fund may be reimbursed to the extent possible from the proceeds from the sale of additional bonds issued to capitalize the cost of additions or betterments, which have been paid out of this fund.

Any unused portion of the Capital Fund should be carried forward for use in subsequent years, provided that any funds not so used within five years from the date of [fol. 630] their origin may be employed in the discretion of the Board of Directors for the retirement of the funded debt of the company.

Likewise the annual depreciation charge on equipment must be unquestionably set aside in a special cash fund and used only to take care of interest and principal payments on Equipment Trust obligations now outstanding or hereafter issued, and to take care of in whole or in part the purchase, building or improvement of equipment. Any unused portion of this fund should be carried forward for use as above outlined in subsequent years, provided that any part of said fund not used may, in the discretion of the directors, be transferred to the Capital Fund above described.

It is for the ultimate interest for each class of security holders, as well as the public, that any plan approved should err on the side of conservatism rather than on the side of overissue of securities, particularly of fixed interest obligations. The above provisions in respect to capital fund and depreciaion would eliminate as far as possible the temptation of the future managements to bleed the adequate upkeep of the property in order to pay interest or dividends—a temptation that past managements have been unable to resist—and in addition insure the necessary upkeep and maintenance of roadway and equipment at all times.

The fact is that the Rio Grande system has expended for additions and betterments to roadway an average of [fol. 631] $1,489,420.00 annually during the past fifteen years, while charges to operating expenses incident to improvements on the Rio Grande have averaged $882,835.00 annually for fifteen years. Charges to operating expenses incident to improvements on the Salt Lake have averaged $80,735.00 annually for the past twelve years. Thus over an extended period charges to operating expenses incident to improvements on the consolidated properties have averaged $963,570.00. Any new management expending this capital fund in the efficient manner the Trustees have used in their maintenance work, i. e., by mechanical methods and in a permanent manner, can make considerable savings in the expenditure of these capital and depreciation funds.

In reference to the allocation of the securities of the reorganized company, the Interstate Commerce Commission plan calls for a maximum of $29,403,144.00 in first mortgage four per cent fixed interest bonds. (a) $7,443,680.00 (the exact figure) of these bonds should be first set aside for sale at par to the Reconstruction Finance Corporation for the remaining cash necessary to carry out the terms of the Interstate Commerce Commission plan. (b) Special treatment should be given to the old advances of the Reconstruction Finance Corporation, partly as a consideration for the purchase for cash at par of the bonds specified in (a) above, and partly because of the strategic value of the collateral pledged to secure the same.

Attached hereto and marked Exhibit A is a distribution [fol. 632] of securities sheet, with the adjustments hereinabove suggested, carried through to the junior securities as of January 1, 1941, all within the framework of the Commission plan. After giving effect to these adjustments, the securities of the reorganized company are allocated to the various mortgage divisions and creditors in proportion and in accordance with the priorities as determined by the Commission plan. It is believed that the effective date of the plan should be moved forward to the termination of the next preceding semi-annual period.

The plan of reorganization (printed record p. 5164) and M of the order of the Interstate Commerce Commission based thereon (printed record p. 5196) provide for a reorganization committee of five members to carry out the plan.

In the opinion of the Commission (printed record p. 5164), such committee is necessary.

Subsection f of Section 205, Title 11, U. S. C. A., provides "Upon confirmation of the plan the debtor, and any other corporation or corporations organized or to be organized for the purpose of carrying out the plan, shall have full power and authority to, and shall, put into effect and carry out the plan and the orders of the judge relative thereto, under and subject to the supervision and control of the judge."

There is nothing in the Act specifically referring to a reorganization committee, except perhaps Subsection c-12, which provides for the compensation of reorganization managers and committees, but the Act seems to assume such [fol. 633] a committee will be created to carry out the plan, but, as seen, it must be under the supervision and control of the judge. Furthermore, the Commission plan delegates to the court the right to correct any defects, supply any omissions or reconcile any inconsistencies that may be necessary to carry out the plan effectively.

The property of the debtor and secondary debtor is located almost wholly in the States of Colorado and Utah, and I therefore firmly believe the provisions of the plan for a reorganization committee should be modified so as to require that members of the committee representing the various interests, as provided for, shall be residents of Colorado or Utah, subject to the approval of the Commission or the court, or both, and that all meetings and proceedings of the committee should be held in Denver, Colorado, at the main office of the debtor, and that counsel for the committee, if any are necessary, shall be appointed by the court. These modifications are necessary in the opinion of the court to promptly expedite the carrying out of any plan finally adopted, and closing the proceeding and restoring the debtor to its rightful owners.

It is suggested in the brief on behalf of the Insurance Group Committee that, looking to practical results, any reorganization of a railroad requires readjustments of numerous contractual rights and interests between various groups of creditors, to the end that the final plan may be fair and equitable to all creditors and compatible with the public interest. It is suggested that these results cannot readily [fol. 634] be attained under the legalistic procedure at arm's length. It is further stated that at the proper stages in

a proceeding such as this it is desirable that the public interest be definitely represented by some authoritative agency. The writer of the brief further states it is to be regretted the statute did not provide for some such informal meeting of the representatives of the various classes of security holders participating in the hearings, and by conference and negotiation under the direction of the Commission seek to arrive at an adjustment of these questions and any other issues involved.

This suggestion is a happy one, and I suggest that if upon assembling in Denver, January 6th it is thought best that all the parties go into a conference, the court will be glad to name some one to represent the court and public to see if a plan consonent with the views here expressed and the Interstate Commerce Commission plan cannot be agreed upon. Otherwise the court may disapprove the plan and return it to the Commission for the reasons herein stated.

J. Foster Symes.

December 6, 1940.

(Here follows 1 paster, folios 635-636)

[fol. 635–636]

EXHIBIT "A"

The Denver and Rio Grande Western Railroad Company Reorganization Plan

Distribution of New Securities as of January 1, 1941

Present Liabilities	Principal Amount[1]	Accrued Interest	Total	Cash from Connecting Carriers	Undisturbed	50 Yr. 1st Mortgage 4's Fixed	Percent	75 Yr. Income 4½% Bonds, Series A	Percent	Preferred Stock 5%	Percent	Common A	Percent	Common Ball to Connecting Carriers for $10,000,000 Cash
Trustees' Certificates	$5,000,000	$	$ 5,000,000	$ 5,000,000	$	$		$		$		$		$
Reorganization Expense	1,000,000		1,000,000	1,000,000										
Equipment Trusts[2]	5,789,000		5,789,000		5,789,000									
Rio Grande Western 1st Trust 4's	15,190,000	3,645,600	18,835,600			5,488,112	29.14%	13,347,488	70.86%					
Rio Grande Western 1st Cons. 4's	15,080,000	3,770,000	18,850,000							18,850,000	100.00%			
Rio Grande Junction Bonds, 5%	2,000,000	558,333	2,558,333			745,419	29.14%	1,812,914	70.86%					
D&RG 1st Cons. 4's and 4½'s	41,169,000[3]	10,911,365	52,080,355			5,311,112	10.20%	14,112,375	27.10%	9,574,150	18.38%	23,082,718	44.32%	
D&RGW Ref. and Imp. 5's and 6's	20,096,000[4]	6,405,000	26,501,000			2,702,551	10.20%	7,181,058	27.10%	4,871,790	18.38%	11,745,601	44.32%	
D&RGW Gen. Mortgage 5's	29,808,000	10,681,200[5]	40,489,200									3,076,581	7.60%	
R.F.C. Notes	10,691,850	2,161,934	12,853,784			7,712,270	60.00%	5,141,514	40.00%					
Denver and Salt Lake Bonds[6]	11,234,000		11,443,680[6]	4,000,000		7,443,680								
Chase National Bank Loan[6]	1,500,000	478,458	1,978,458		1,978,458									
Railroad Credit Corp. Loan[7]	206,291		206,291		206,291									
Denver and Salt Lake Minority Stock	4,111 shares		411,100					411,100						
Total			$197,996,801	$10,000,000	$7,973,749	$29,403,144		$42,006,449		$33,295,940		$37,904,900		$10,000,000
Annual Fixed Charges					Note 8	$1,176,126								
Annual Contingent Interest								$1,890,290						
Annual Preferred Stock Dividend										$1,664,797				

[1] Excluding bonds pledged with R. F. C., but including bonds pledged as collateral for Chase Bank loan ($6,096,000 R&I 5's) and Railroad Credit Corp. loan ($662,000 D&RG 1st Cons. 4's).

[2] Including $1,260,000 Equipment Trust Series G Certificates authorized by Court, to be issued February 1, 1941.

[3] Excluding $7,452,000 of contingent interest accrued in five year period ended February 1, 1929, and excluding 50% payment which was made on coupon due February 1, 1934.

[4] Excluding $1,266,000, principal amount, pledged with R.F.C., to be canceled.

[5] Includes redemption premium of 1% on First Mortgage Bonds and 2% on Income 6's.

[6] New securities to be issued as collateral for Chase Bank note in exchange for bonds now pledged: New 1st 4's, $816,102; Income 4½'s, $2,168,271; Preferred Stock, $1,470,584; Common A, $3,546,043. Interest on Chase Bank note computed in accordance with claim of Bank at 6% from date petition filed under Sec. 77, as provided by laws of State of New York. Subject to final determination.

[7] New securities to be issued as collateral for Railroad Credit Corp. loan in exchange for bonds now pledged: New 1st 4's, $85,680; Income 4½'s, $226,047; Preferred Stock, $153,311; Common A, $369,682. In computing amount due Railroad Credit Corp., amount due D&RGW as participating carrier in Marshalling and Distributing Plan has been deducted.

[8] Interest on undisturbed securities will be treated as follows: Interest on Equipment Trust Certificates, 1941, $138,076, reducing annually as principal installments are paid, to be paid in cash. Interest on Chase Bank note payable out of interest on collateral. Interest on Railroad Credit Corp. note, $8,251.64 per annum.

Filed Dec. 14, 1940—
George A. H. Fraser, Clerk.

[fol. 637] PETITION OF CENTRAL HANOVER BANK AND TRUST COMPANY AS TRUSTEE

EXHIBIT "A"

"DISCUSSION PLAN" FOR D. & R. G. W.

A. Origin

In his interim order of August 30, 1940, Judge Symes clearly indicated that he expected the parties to attempt the negotiation of an agreed plan, for presentation to the Court before the next hearing.

After receipt of the Judge's aforesaid interim order, the R. F. C., at the instance of the Insurance Group Committee, made available to the latter a study which had been made by its Railroad Division, as the basis for such a compromise plan. The present proposal has been evolved after several conferences between the R. F. C. and the Group's subcommittee. Referred to herein as the "Discussion Plan", it embodies the allocations determined upon by that subcommittee, with certain modifications suggested by the representatives of the R. F. C.

It is presented at this meeting in the hope that it will be acceptable to all interests as a compromise plan which may be carried out with a minimum of delay and without expensive litigation.

B. Capitalization

The Discussion Plan is based on the assumption that the connecting railroads desiring control will purchase $4,000,000 Series B Income 4½s at par and 60,000 shares of Class B Common Stock (having the exclusive power of ordinary management somewhat along the general lines of the Insurance Group 1937 plan) at $100 per share or for $6,000,000. This $10,000,000 cash will be used to retire $5,000,000 Trustee's Certificates, furnish $1,000,000 working capital, and provide for the cash offer hereinafter stated to the D. S. L. Income Bonds.

[fol. 638] In so far as it has been practicable to do so and at the same time produce a plan that will have a chance of meeting with the approval of security holders, the plan is based upon the I. C. C. plan, in this respect complying with Judge Symes' interim order. Total capitalization of

approximately $147,000,000 fixed charges, and total fixed and contingent charges are substantially the same as in the original I. C. C. plan.

The capital structure is to be slightly different in that there will be two series of Income bonds—$6,905,788 Series A 4s and about $36,000,000 Series B 4½s (includes $1,387,967 which is the contingent portion of the Chase 4% note). There will be about $5,000,000 less Preferred stock and there will be two classes of Common stock with the total Common stock being increased by 60,000 shares of no par Class B Common which offsets the reduction in Preferred stock, and 43,970 shares of no par Class A Common.

The new capitalization is stated on Schedule 1 hereto and annual requirements thereunder are stated in Schedule 2 hereto. The series A Incomes will have a term of 20 years and bear interest at 4% (cumulative for 4 years) payable after the Capital Fund, but before interest on Series B, and will be exclusively entitled to a sinking fund of ¼% on maximum prior issue of Income Bonds (payable after Series B interest); upon retirement of Series A, the sinking fund will apply to Series B.

C. Allocations

Detailed allocations are shown on Schedule 3 hereto. Attention is called to the following:

The plan provides that the R. G. W. First Trusts and the Rio Grande Junction Firsts be given 100% of their [fol. 639] claim for principal and interest in new First 4s as compared with 100% in Income bonds which the I. C. C. Plan proposed.

Under the plan, the R. F. C. will receive approximately 1% of its claim (of $11,177,179) in cash, about 58% in First 4s, and about 41% in Income A 4s and will not be called upon to furnish any cash for the reorganization. The amount of cash R. F. C. will receive under the plan will be increased and the amount of First 4s decreased to the extent that the D. S. L. Income bondholders accept new First 4s in lieu of cash, as hereinafter set forth.

The Eastern Consol 4s and 4½s are to receive 5% of their claim in new First 4s or at approximately the same rate per mile for the mortgage's 60 odd miles in the Western end of the system as the rate per mile for which new First

4s are offered the Junctions. The I. C. C. Plan gave no First 4s to the Eastern Controls but did propose 35% in Incomes. Since the Discussion Plan has given 5% to this mortgage in new First 4s, their allocation of Series A and Series B Income 4½s is reduced to 31.5%, which makes a total of 36.5% in bonds. The allocation of Preferred stock to the Eastern Consols is 25%, as in the I. C. C. Plan, and 32.7% has been allotted in Class A Common stock (reduced from 40% in I. C. C. Plan because of increase of 1½% in bonds).

The Refunding and Improvement 5% and 6% bonds were given, in the I. C. C. Plan, the same treatment as was given the Eastern Consols and the Discussion Plan accordingly accepts this measure of relative value and offers the R. & I.'s the same improved treatment proposed for the Eastern Consols except that an additional 5% in Preferred stock is allocated to R. I.'s to compensate for the Series A Incomes given to the Eastern Consols.

[fol. 640] The Western Consol 4s are offered 36.5% in Income B 4½s and 63.5% Preferred stock as against no Income bonds in the I. C. C. Plan, which gave them 100% in Preferred stock. Since the I. C. C. Plan gave the Western Consols 100% in the next junior security to that offered The Western Firsts, it might be contended they should have 100% in Income bonds. However, since other plans proposed practically the same treatment for the Eastern and the Western Consols in the most senior security offered these mortgages, the proposal in the Discussion Plan provides for this similarity of treatment. Under the plan the Eastern Consols, the Western Consols, and the R. & I.'s each receive 36½% in new bonds. This is a concession to the R. & I's, giving them treatment better than they are given in the I. C. C. Plan, which they supported at the court hearing.

The D. & R. G. W. General 5s are offered much better treatment than in the I. C. C. Plan, 42.5% of their claim in Class A Common stock.

The R. C. C. and the Chase Bank notes are to be extended, as was proposed by the I. C. C., but their collateral will be improved because of the better treatment given the securities now pledged. These note holders either advised the Court that the less favorable I. C. C. Plan was acceptable, or failed to oppose.

The D. S. L. First 4s outstanding in the amount of $1,500,000 and maturing in 1950 are to remain undisturbed instead of being called, as was proposed by the I. C. C.

The D. S. L. Incomes are to be offered 40% in cash or new First 4s and 60% in new Income B 4½s, contingent upon the acceptance of this offer by substantially all the [fol. 641] holders. To the extent that these holders elect to take new First 4s, in lieu of cash, additional cash will be available for application against the R. F. C. claim.

The D. S. L. minority stockholders were offered 100% of their par value in Income 4½s by the I. C. C. and this treatment is continued.

The treatment accorded the security holders who are offered Preferred is improved over the I. C. C. Plan because, among other things, there is to be a smaller amount of Preferred outstanding with resultant greater earnings per share from a similar amount of income available for Preferred dividends.

October 28, 1940.

[fol. 642]

SCHEDULE "I"

The Denver & Rio Grande Western Railroad Company

Capitalization in "Discussion Plan"

(Effective Date of Plan—June 30, 1938)

	Principal		
	Amended I. C. C. Plan	Original I. C. C. Plan	Discussion Plan
Equipments	$2,795,000	$2,795,000	$2,795,000
First Mortgage 4's	29,403,144	29,403,144	29,336,500
R. C. C. Loan 1½%	278,000	278,000	278,000
Chase Note 4%	.....	1,749,917	[1]361,950
D. & S. L. Extended First 4's	.....	.....	1,500,000
Total Fixed Interest Debt	$32,476,144	$34,226,061	$34,271,450
Income Mortgage A 4's	.....	.....	6,905,788
Income Mortgage B 4½'s	42,006,449	42,006,449	34,327,506
Chase Note 4%[2]	1,749,917	.....	1,387,967
Total Contingent Int. Debt	$43,756,366	$42,006,449	$42,621,261
Total Debt	$76,232,510	$76,232,510	$76,892,711
Preferred Stock 5%	33,295,940	33,295,940	27,801,110
Common Stock Cl. A[3]	37,904,904	37,904,904	[4]35,956,615
Common Stock Cl. B[3]	.....	.....	6,000,000
Grand Total[5]	$147,433,354	$147,433,354	$146,650,436

[fol. 643]

Schedule 1 (Cont'd)

	Per Cent of Capitalization		
Fixed Int. Debt[1]	22.0	23.2	23.4
Cont. Int. Debt	29.7	28.5	29.0
Total Debt	51.7	51.7	52.4
Preferred Stock	22.6	22.6	19.0
Common Stock	25.7	25.7	28.6
Grand Total	100.0%	100.0%	100.0%

Note 1—Fixed interest proportion.
Note 2—Contingent interest proportion.
Note 3—No par value stock calculated at $100 per share.
Note 4—Based on value of $85 per share.
October 28, 1940.

[fols. 644-645]

SCHEDULE 2

The Denver & Rio Grande Western Railroad Company.

Annual Requirements in "Discussion Plan"

	Amended I. C. C. Plan	Original I. C. C. Plan	Discussion Plan
Equipment Trust	$98,243	$98,243	$98,243
1st Mtge. 4's	1,176,126	1,176,126	1,173,460
R. C. C. Loan 1½%	4,170	4,170	4,170
Chase Note 4%		69,997	14,478
D. & S. L. Ext. 1st 4's			60,000
Total Fixed Int.	$1,278,539	$1,348,536	$1,350,351
Capital Fund	750,000	750,000	750,000
Prior to Contingent Int.	$2,028,539	$2,098,536	$2,100,351
Income Mtge. A 4's			276,232
Income Mtge. B 4½'s	1,890,290	1,890,290	1,544,738
Chase Note 4%[2]	69,997		55,519
Total Contingent Int.	$1,960,287	$1,890,290	$1,876,489
Income Mtge. Sinking Fund	105,016[3]	105,016[3]	69,388[4]
Prior to Deferred Dividend	$4,093,842	$4,093,842	$4,086,228
Preferred Dividend 5%	1,664,797	1,664,797	1,390,056
Prior to Cl. A Common	$5,758,639	$5,758,639	$5,476,284

Note 1—Fixed interest proportion.
Note 2—Contingent interest proportion.
Note 3—¼ of 1% on outstanding Income Bonds plus interest on bonds in sinking fund.
Note 4—¼ of 1% on outstanding and pledged Income bonds without interest on bonds in sinking fund.
October 28, 1940.

[fol. 646]

SCHEDULE 3

The Denver & Rio Grande Western Railroad Company

Distribution in "Discussion Reorganization Plan"

	Total Claim June 30, 1938	Cash	Undistributed or Extended	50 Year 1st Mtg. 4's	20 Year Income 4's, Series A	75 Year Income 4½'s Series B	5% Pfd. Stock	Class A Common (Shares)	Class B Common (Shares)
Equipment Obligations	$2,795,000		$2,795,000						
R. G. Western 1st Trust 4's	17,316,600			$17,316,600(100%)					
R. G. Western Consol. 4's	17,342,000					$6,329,830(36.5%)	$11,012,170(63.5%)		
Junction 1st 5's	2,308,333			2,308,333(100%)					
D. & R. G. Consol. 4's	39,585,000			1,979,250(5%)	$1,979,250(5%)	10,490,025(26.5%)	9,896,250(25%)	$152,402.25(38.5%)	
D. & R. G. Consol. 4½'s	7,530,760			376,538(5%)	376,538(5%)	1,995,651(26.5%)	1,882,690(25%)	28,993.43(38.5%)	
D. & R. G. W. Ref. & Imp. 5's	14,250,000			712,500(5%)		4,488,750(31.5%)	4,275,000(30%)	47,737.50(33.5%)	
D. & R. G. W. Ref. & Imp. 6's	2,450,000			122,500(5%)		771,750(31.5%)	735,000(30%)	8,207.50(33.5%)	
D. & R. G. W. Gen. 5's	37,135,800							185,679.00(50.0%)	
R. F. C. Notes	11,177,179	$106,400(95%)		6,520,779(58.34%)	4,550,000(40.71%)				
D. & Salt Lake 1st 4's	1,500,000		1,500,000(100%)						
D. & Salt Lake Incomes	9,734,000	3,893,600(40%)				5,840,400(60%)			
D. & R. G. W. Trustees Ctfs.	5,000,000	5,000,000							
Chase Nat. Bank Loan	1,749,917		(1) 1,749,917	(2) 361,950		(3) 1,387,967			
R. C. C. Loan—1½%	278,000		278,000						
Reorgan. Expenses etc.	1,000,000	1,000,000							
D. & S. L. Minority Stock	411,100					411,100			
Purchasing Railroads						(4) 4,000,000(5)			(6) 60,000
Total		$10,000,000	$4,573,000(7)	$29,698,450(8)	$6,905,788	$35,715,473(9)	$27,801,110	$423,019.68	$60,000
Cumulative new capitalization (assuming common Stock Class A @ $85 and Class B @ $100 per share)			4,573,000	34,271,450	41,177,238	76,892,711	104,693,821	140,650,436	146,650,436
Fixed interest charges			162,413(10)	1,187,938(11)					
Cumulative fixed interest charges			162,413	1,350,351					
Capital fund				750,000					
Contingent interest charges					276,232	1,600,257(12)			
Cumulative interest charges and capital fund			162,413	2,100,351	2,376,583	3,976,840			
Sinking fund and preferred dividends						109,388(13)	1,390,056		
Grand total all charges and dividends			162,413	2,100,351	2,376,583	4,086,228	5,476,284		

Note 1—To be a 4% note secured by pledge of following for claim of $7,239,000 on pledged R. & I.'s—

New 1st 4's	$361,950	New 5% Pfd. Stk.	$2,171,700
New Inc. B 4½'s	2,280,285	New Com. Stk. "A"	27,250.65 shs.

Note 2—Excludes principal amount of Chase Note of $1,749,917 which for purposes of determining outstanding capitalization, fixed charges and contingent charges shall be considered as a 4% fixed interest note of $361,950 and a 4% contingent interest note of $1,387,967.

Note 3—For an aggregate of $10,000,000 cash to be applied as shown in Column entitled Cash.

Note 4—Consists of:

Equipment Trust	$98,243
Railroad Credit Corp.	4,170
D. & S. L. 1st 4's	60,000
	$162,413

Note 5—To be pledged but interest to be payable thereon.

Note 6—Includes $361,950 to be pledged under Chase Note—actual amount of First 4's to be outstanding will be $29,3..,500.

Note 7—Consists of $1,173,460 interest on $29,336,500 outstanding First 4's and $14,478 interest on $361,950 First 4's to be pledged under Chase Note.

Note 8—Portion of Chase Note upon which interest at 4% will be contingent depending upon payments made on collateral under Chase Note.

Note 9—Includes proportion of Chase Note upon which interest at 4% will be contingent—actual amount of income 4½'s to be outstanding will be $34,327,506.

Note 10—Consists of: $1,544,738 interest on $34,327,506 income 4½'s to be outstanding.
55,519 interest at 4% on $1,387,967 proportion of Chase Note to be contingent.
$1,600,257 Total

Note 11—¼ of 1 per cent on outstanding and pledged ~~Series A and~~ Series B income bonds.

October 28, 1940

[fol. 647] Memorandum Re Discussion Plan for D. & R. G. W.

It appeared to those attempting to work out a plan acceptable to all interests that after exploring numerous approaches to a compromise plan that there were two limitations which must be observed in order to work it out. First, that the charges and capitalization should conform to those set up by the I. C. C. Plan and second, that if that were done it would not be possible to use first mortgage bonds to raise the necessary new money. The Discussion Plan conforms to these two requirements and it is believed represents an equitable comparative treatment between the various issues.

The following important points should be noted concerning the capitalization of the Discussion Plan. The effective date is the same as that of the I. C. C. Plan namely, June 30, 1938. The total fixed interest debt is $34,271,450, which is only $45,399 more than that originally approved by the Commission, and the fixed charges have been increased only by the amount of $1,815 per annum, which is negligible. The total contingent interest debt to be issued is $42,621,261, against $42,006,449 as approved by the Commission, or $614,812 more. However, due to the use of a Series "A" bond, contingent interest charges have been reduced to an amount which is $13,801 less than those proposed in the I. C. C. Plan. The over-all charges on debt, fixed and contingent, have been reduced by approximately $12,000. Total charges prior to preferred dividends were $4,086,228 compared to $4,093,842 under the I. C. C. Plan.

It should also be noted that two material departures from the I. C. C. Plan do not violate the I. C. C. restrictions on capitalization, but bring about changes that appear to [fol. 648] be a real benefit to the property. The first change is that the income bonds are divided into two series, instead of being all of one as proposed by the I. C. C. A small issue, $6,905,788 Series "A" bonds bearing a 4% coupon, come due in twenty years and have the full benefit of the total income bond sinking fund. The second change is a decrease of approximately $5,500,000 in the amount of preferred stock to be issued, and the issuance in its place of 60,000 shares of Class "B" stock to be sold, together with $4,000,000 Series "B" income bonds, to the eastern connections for the purpose of raising the necessary $10,000,000 through non-fixed interest bearing securities.

Another departure from the Commission Plan is an increase of about 47,000 shares Class "A" common stock brought about by an effort to increase a quantitative recognition of general mortgage bonds.

To reiterate the essential points of the capitalization, the Discussion Plan fixed charges are $1,815 higher than that originally set by the Commission. But the charges through the contingent interest debt are $11,980 less. Total charges prior to the preferred dividends including capital fund and sinking funds are $7,614 less than under the I. C. C. Plan. Dividend requirements on the preferred stock are almost $275,000 less under the Discussion Plan. The total capitalization proposed, taking the no-par stock at $100 a share, is $152,995,521 against $147,433,354 proposed by the I. C. C. Plan. But, if the no-par is taken at $88.28 per share, the total capitalization is exactly that proposed by the I. C. C.

The negotiations with reference to the Discussion Plan have so far progressed only to the working out of difficult and controversial questions relating to capitalization and allocation of securities. There remain to be worked out, [fol. 649] however, details of provisions with reference to the earmarking of funds to be used only for expenses incident to roadbed and structures and for depreciation charges on equipment. It is believed that such matters can best be developed after informal discussion with the Court in order that a more clear understanding may be obtained as to his views on these matters.

Denver & Rio Grande Western

Extent to Which "Discussion Plan" Conforms with I. C. C. Plan

1. Effective date to be June 30, 1938—same as I. C. C. Plan.

2. Equipment Trusts of $2,795,000 to be undisturbed—same as I. C. C. Plan.

3. First Mortgage 4's to be outstanding—

Discussion Plan	$29,336,500.
I. C. C. Plan	$29,403,144.

4. R. C. C. Loan of $278,000 to be extended or paid—same as I. C. C. Plan.

5. Chase Note of $1,749,917 to be extended and secured by securities issuable for present collateral and interest of 4% to be paid if earned from payments on new collateral —same as I. C. C. Plan.

6. Total fixed interest debt and fixed charges thereon—

	Principal	Annual Charges
Discussion Plan	$34,271,450	$1,350,351
Original I. C. C. Plan	34,226,061	1,348,536
Amended I. C. C. Plan	32,476,144	1,278,539

It is important to direct attention to the fact that the I. C. C. found and stated in a tabulation on Page 61 (mimeographed copy) of its original report dated July 11, 1939, [fol. 650] that fixed charges should be $1,348,536 and the maximum capital fund deduction should be $750,000. These two would total $2,098,536. Then on Page 63, the I. C. C. stated—"Under the plan herein approved the fixed interest requirements, plus the maximum payment into the capital fund, would amount to $2,098,536, subject to some possible increase in the amount of first mortgage bonds issued in the reorganization, as has been indicated."

The I. C. C. report then states in the first complete sentence on Page 64 of the same report—

"We find that, after due consideration of the probable future earnings of the properties in the light of their earnings experience and other relevant facts, there will be adequate coverage of these fixed charges of the new company by the probable earnings for the payment thereof."

It so happened that the I. C. C. erroneously assumed it had allocated all the securities upon which these fixed charges of $1,348,536 would be payable. When the I. C. C. was advised of its error of including $69,997 interest on the Chase Note as a fixed charge instead of a contingent charge, it did not revise or change its finding that fixed charges of $1,348,536 would be adequately covered but made only the following statement on page 18 (mimeographed copy) of its report dated April 2, 1940—

> "In the summary of the approved plan, 233 I. C. C. 515,593, the annual interest on the extended (Chase) note was shown as a fixed interest charge. In the revised summary of the plan, shown later herein, such interest is included as a contingent charge."

In other words, the I. C. C. did not allocate all the fixed interest obligations which it found could be issued. In [fol. 651] view of the I. C. C.'s actual finding on the record, which the technical error did not change, the Discussion Plan adopted a fixed charge of $1,350,351 or within $1,815 of the I. C. C. finding.

7. Maximum annual deduction of $750,000 to be made for capital fund before payment of contingent interest—same as I. C. C. Plan.

8. Income Mortgage bonds to be issued in two series ($6,905,788 Series A 4's and $34,327,506 Series B 4½'s) but to be outstanding in the aggregate as follows—

	Principal	Annual Interest
Discussion Plan	$41,233,294	$1,820,970
Original I. C. C. Plan	42,006,449	1,890,290
Amended I. C. C. Plan	42,006,449	1,890,290

9. Total fixed and contingent interest debt and annual requirements thereon to be as follows—

	Principal	Annual Interest
Discussion Plan	$76,892,711	$3,226,840
Original I. C. C. Plan	76,232,510	3,238,826
Amended I. C. C. Plan	76,232,510	3,238,826

10. Annual sinking fund on Income Bonds to ¼ of 1% on outstanding and pledged Income Bonds plus interest on bonds in sinking fund, payable if earned after payment of contingent interest, amounting to—

	Sinking Fund
Discussion Plan	$109,388
I. C. C. Plan	105,016

11. Total charges prior to Preferred Dividends—

Discussion Plan	$4,086,228
I. C. C. Plan	4,093,842

[fol. 652] 12. Total Preferred and Common Stock, if the no par Common Stock in Discussion Plan, both Class A and Class B, be taken at the balancing figure of $88.28 per share, required to make the total capitalization under the Discussion Plan conform with the capitalization in the

I. C. C. Plan which calculated the no par Common Stock at $100 per share—

	Total Preferred & Common Stock	
	Shares	Arbitrary Stated Value
Discussion Plan	761,028	$70,540,643
I. C. C. Plan	712,008	71,200,844

13. Total capitalization to be as follows—

Discussion Plan:

Calculating no par stock at $100 per share	$152,995,521
Calculating no par stock at $88.28 per share	147,433,354

I. C. C. Plan:

No par stock at $100 per share	$147,433,354

October 28, 1940.

Denver & Rio Grande Western

Changes from I. C. C. Plan of Reorganization

1. Issuance of two series of Income Bonds under the Discussion Plan as follows:

$6,905,788 Series A 4%, due in 20 years, secured equally as to principal with $34,327,506 Series B 4½% bonds, due in 75 years, but entitled to interest prior to Series B bonds and also entitled to all Income Bond sinking fund payments until all Series A bonds have been retired. Interest on [fol. 653] the Series A and Series B bonds to be cumulative to the extent of 4 years interest as in the I. C. C. Plan but the rights to cumulation under the Discussion Plan do not begin until the plan actually becomes operative.

2. Issuance of $5,494,830 less Preferred stock under the Discussion Plan as follows:

	Preferred Stock
Discussion Plan	$27,801,110
I. C. C. Plan	33,295,940
Difference	$5,494,830

3. Issuance of two classes of Common Stock under the Discussion Plan or the creation of 60,000 shares of Class B stock to be sold for $6,000,000 to the eastern connecting lines desiring control, the proceeds to be used to retire $5,000,000 trustee certificates and to provide $1,000,000 working capital.

4. Sale of $4,000,000 Series B 4½% Income Bonds to the eastern connecting lines desiring control, the proceeds to be used to provide an alternate offer of $4,000,000 cash to the holders of Denver and Salt Lake Income bonds instead of $4,000,000 in new First Mortgage bonds of the reorganized company.

5. No new First Mortgage bonds to be sold for cash in contrast to sale of about $17,500,000 First Mortgage bonds to the R. F. C. under the I. C. C. Plan.

6. Denver and Salt Lake First Mortgage 4% bonds outstanding in the amount of $1,500,000 and due in 1950 to remain undisturbed whereas I. C. C. Plan provided for their redemption at the call price of 101 or for $1,515,000. This means the new Denver & Rio Grande Western First [fols. 654-655] Mortgage would not be a first lien on the Denver & Salt Lake property until they were redeemed which would probably be prior to 1950.

7. Distribution of new securities to the various security holders would be different, all as outlined in a separate schedule. This was required in order to have a Plan which would meet with the approval of all security holders.

October 28, 1940.

Filed Jan. 6, 1941—George A. H. Fraser, Clerk.

[fol. 656] In United States District Court

Opinion—March 6, 1941

RE D & R G

This matter was last before the Court January 6, 1941, for final arguments following the testimony given at the hearing in August. Since then numerous conferences of the parties have been held in New York. The Court, hap-

pening to be sitting in New York at the time by assignment, attended two of these on January 30th and 31st, and was furnished with the so-called FitzGibbon Plan, which was there discussed. This plan differs substantially from the Interstate Commerce Commission Plan, and the views [fol. 657] of the Court (Opinion of Dec. 6, 1940), particularly in the treatment of the Reconstruction Finance Corporation's claim, that of the Rio Grande Western First Trusts, the Rio Grande Junction bonds and the Denver & Salt Lake Income 6s.

This so-called FitzGibbon Plan is reputed to be agreeable to the so-called Insurance Group, and is the first indication of a recession from their insistence that the Rio Grande Western First Trust 4s and the Junction First 5s receive 100% in first mortgage bonds. They further indicated a willingness to take 78% of their claim in new first mortgage bonds and the balance in income bonds.

At all hearings before the Court since the Interstate Commerce Commission plan was certified, the objections of the so-called Insurance Group have been a stumbling-block to every suggested compromise plan, they insisting from the very beginning that the Western Divisional Mortgages receive 100% in first mortgage bonds. This group represents a vertical rather than a horizontal section of the debtors' obligations, and actually a small minority interest of any one issue.

The arguments, pro and con, on their objections have been repeated so many times it is unnecessary to set them forth here, but it is hoped they will not go so far as to oppose the plan herewith submitted, or any modification thereof the Commission may see fit to recommend, bearing in mind the main reason the Court rejects the Interstate [fol. 658] Commerce Commission plan is its failure to give due recognition to the preferred position of the Rio Grande First Trust 4s and the Junction 5s, as compared to the Reconstruction Finance Corporation notes. Had these mortgage trustees and institutional owners of the securities of this property shown the same interest in the debtor before this petition in reorganization was filed as they have since, this whole proceeding might well have been prevented with the resulting losses the securityholders must now make up their minds to take. This group, by means not disclosed, have assumed a position of importance and influence in the reorganization proceedings out of all proportion to the

amount of securities they represent, and the question might properly be asked: Are they in a position to represent fairly in this proceeding three different sets of bondholders whose interests are in many respects conflicting?

This FitzGibbon Plan must be rejected for the same reasons that the Court rejected the so-called Discussion Plan, (Opinion of Dec. 6, 1940), i. e., it is not within the framework of the Interstate Commerce Commission plan; fails to provide the new cash necessary to carry it out; fails to give equitable treatment to the Divisional Mortgages as determined by the Interstate Commerce Commission, greatly favoring the Western First Trust 4s, largely at the expense of the Rio Grande Consolidated 4s and 4½s; and is presented without any assurances of acceptance by the parties. [fol. 659]. Anticipating, perhaps, the objection that it fails to provide necessary cash to carry out the plan, it was later suggested as part of this plan that the necessary cash, to wit, $5,000,000.00 required to pay off outstanding Trustees' Certificates, and $1,000,000.00 for reorganization expenses, be supplied by sale of a new Class B common stock with sole voting power to the three eastern connecting roads, the Rock Island, Missouri Pacific and Burlington. However, before other railroads could purchase this stock, the Interstate Commerce Commission would have to grant its approval, and the proponents of the plan do not offer any assurance that binding commitments to purchase the stock or the approval of the Interstate Commerce Commission have been or can be obtained.

As an alternative it was stated that $3,000,000.00 is available from the cash balance in the hands of the Trustees and that the Reconstruction Finance Corporation purchase sufficient new income bonds for cash to finance the plan. The Trustees of the debtor state their income forecast for the coming year, taking into account expenditures authorized by the Court and on the assumption that the new locomotives authorized by order of February 10, 1941, are to be paid for to the extent of 75% by an equipment trust, shows an estimated cash balance on December 31, 1941, of $2,748,000.00. The Trustees and the Court, however, feel unless too strong objection is made by the interveners, that these new locomotives should be paid for in cash in full, with- [fol. 660] out at this time incurring additional indebtedness in the form of equipment trusts. This would require

$848,750.00, in addition to the down payment included in the forecast, and would deplete cash on hand by that amount, leaving a net of $2,900,000.00.

Moreover it is the Trustees' judgment they should have a working balance of not less than $1,250,000.00, for if for any reason the system should face declining traffic, and the Trustees still maintain their present policy towards work on the line and the acquisition of new equipment, this balance is the only shock-absorber against any shrinkage in gross. In addition it is wise to keep a substantial cash balance and assure, under any circumstances, the payment of Trustees' certificates at maturity, which occurs within the next five years, if the railroad is not reorganized within that time. For these reasons no part of the Trustees' cash balance is available for reorganization expenses.

The Court (Memorandum of Aug. 30, 1940) agreed in principle with the Insurance Group, holding that "the traffic density on that part of the main line between Dotsero and Salt Lake justifies preferential treatment for the liens secured thereby." In the distribution of securities suggested by the Court (Dec. 6, 1940) the Western First Trusts were given 29.14% of their claims in first mortgage bonds, and the Junctions the same percentage, at the expense of the Reconstruction Finance Corporation and other parties. [fol. 961] It is hoped that all parties will look at the matter from the Court's point of view and bear in mind the Court, with the Commission, is charged with the duty of developing a fair and equitable plan of reorganization. Warren v. Palmer, 310 U. S. 132 (subdivision (e), Sec. 77, Bankruptcy Act).

Considering the public's point of view and that of all creditors, this particular situation requires a consolidation of the Rio Grande and the Denver & Salt Lake, and provisions that will obviate the basic causes that in the past have brought financial disaster to this property, such as application of earnings to fixed charges not earned, with the resulting under-maintenance of the physical condition of the property and its equipment and inability to make net earnings. This is not hard, provided the management, like the Trustees, has the single purpose of the prosperity of this particular property in mind and does not permit its earnings and traffic to be used and diverted, as in the past, for the benefit of other properties.

The holders of Denver & Salt Lake Income bonds are so much better off in their present position than they would be under this FitzGibbon Plan, that it is very doubtful if they would agree to it. Their bonds are neither due nor in default as to the payment of principal and interest, and are to be paid 4% in 1941 out of actual earnings.

It is not the duty of the Court to prepare a plan of reorganization, yet, having carefully studied the Interstate Commerce Commission Plan, including the record before [fol. 662] the Commission, and with the benefit not only of the court proceedings, the briefs and numerous formal and informal discussions and conferences with interested parties and others whom I have consulted, I have concluded that my reasons for not approving the Interstate Commerce Commission Plan can best be indicated by presenting what, in my humble judgment, is a plan that does equity between all the parties, and is well within the requirements of Section 77. Thus the plan annexed hereto represents my views based upon the above experience and study, including the operation of this property during this proceeding and the previous equity reorganization, and it is my best informed, independent judgment.

This plan dated March 1, 1941, effectual as of January 1, 1941, is within the framework of the Interstate Commerce Commission Plan. It makes provision for all cash necessary for its consummation, gives equitable treatment to the Divisional Mortgages in the proportion determined by the Interstate Commerce Commission, which apparently considered divisional earnings and all pertinent facts, more particularly between the Rio Grande First Trust 4s and Rio Grande Consolidated 4s and 4½s. It does not dilute the security of either to provide funds for the retirement of the Salt Lake issues.

In regard to the Salt Lake issues, it calls for the guaranty of the interest on the Firsts and Incomes thereof up to 4% by the reorganized company. The principal of the Salt Lake's debts, including liens for equipment, is left undis- [fol. 663] turbed without assumption by the reorganized company, yet complete consolidation is provided for. The voluntary reduction of interest from 6% to 4% on the Salt Lake Income bonds does not disturb their [illegible]. Four per cent has already been formally declared payable on the

Salt Lake Income bonds for the current year. It neither strengthens nor weakens their existing security, and requires the refunding of non-consenting income bonds. Thus the interest on the Salt Lake Income bonds, which becomes fixed upon consolidation in accordance with the terms of the existing mortgages, is guaranteed up to 4% only by the reorganized company. This 4% interest guaranty merely amounts to a current payment for the use of the Denver & Salt Lake division which, together with the payments required by the assumption of the Tunnel contract, makes available to the new company the Denver gateway, and assures the continuance of the highly competitive bridge traffic and permits the economies of complete consolidation. The new company acquires the Salt Lake Western (the Cutoff) from the Reconstruction Finance Corporation by the payment of the original cost thereof in first mortgage bonds.

The stock of the Salt Lake Western has no bonds ahead of it, so is a first lien next to the rails. The plan provides that the Reconstruction Finance Corporation receive payment for the balance of its collateral loan advances—always a poor risk—in income 4½s, and in addition thereto it is [fol. 664] asked to purchase for new money $6,000,000.00 additional 4½% income bonds. The Reconstruction Finance Corporation is given the privilege of converting as a unit not less than $6,000,000.00 4½% Incomes into Class B common, with full voting power for resale, under certain limitations, to the three eastern connecting carriers.

Thus The Reconstruction Finance Corporation is given a means for liquidating the new money required from it, and in addition for the current collection of its more temporary advances. The total fixed charges, including interest on the Salt Lake to Pueblo division, will be no greater, as shown in ICC Plan. Total fixed charges on the Denver & Salt Lake division, including assumed interest will be greater, but are thought to be justified by the avoidance of any assumption of $11,234,000.00 of principal liabilities.

It is thought this plan meets the principal objection of creditors, especially the Insurance Group, that the security behind the Rio Grande mortgages was being thinned too much to make provision for cash payment of the Salt Lake bonds.

The Court is thoroughly convinced the amount of fixed interest must be kept within the limits of the Interstate

Commerce Commission Plan. This for reasons stated in the previous opinions of the Court, together with the present prospect of increased taxes and labor costs, lessening earnings, and future uncertainties. In the first analysis it [fol. 665] makes very little difference what type of security a creditor gets—whether it calls for payment of fixed or contingent interest or dividends. In no event can the same be paid except out of net income actually earned.

This plan, which, to identify, we will call the plan of March 1, 1941, effective as of January 1, 1941, is within the framework of the Interstate Commerce Commission Plan.

The Court waives its previous insistence that the amount of first lien bonds on the consolidated system be kept within the $29,403,143.00 called for by the ICC Plan, and provides for $41,120,142.00 first mortgage bonds with 3% fixed interest, with an additional 1% contingent, this 1% to be fully cumulative and payable before any interest is paid on the income bonds. At 3% the fixed interest thereon is only $74,000 more than 4% on $29,000,000.00, yet there will be no year when the full 4% will not be earned.

The Rio Grande Western First Trust 4s get 100% of their principal and 80.65% in first mortgage bonds on the full amount of their claim with interest to January 1, 1941.

The Rio Grande Junction bonds receive 101.24% of their principal and 79.14% of their total principal and interest in new first mortgage bonds. Likewise the Eastern Consolidateds receive more equitable treatment than under any [fol. 666] plan heretofore submitted. The increase in these first mortgage bonds reduces the amount of income bonds to $30,289,451.00.

The RFC receives $4,312,853.00 in first mortgage bonds, which equals the amount of their so-called Cutoff notes secured by the Denver and Salt Lake Western stock. This stock, it must be remembered, is really a first mortgage on the Cutoff, there being no bonds or other indebtedness ahead of it. On its old advances the RFC receives $8,540,931.00 in income bonds, and in return is asked to purchase $6,000,000.00 more of 4½% income bonds for cash, to be used to pay the Trustees' obligations and reorganization expenses. In exchange for this, not less than $6,000,000.00 of income bonds held by the RFC may be converted as a unit into the total issue of Class B common stock carrying the sole voting power. Any sum realized by the sale of this Class B stock

or any part thereof by the RFC shall be applied, first, to reimburse it for the par value of the bonds so converted, and, second, to payment at par for cancellation of other income bonds held by the RFC out of holdings received in this reorganization, and any remainder paid to the sinking fund provided for first mortgage bonds. The right to sell this Class B stock by the RFC shall be restricted so that no one purchaser can obtain more than 40% thereof, thus preventing any connecting carrier from controlling the reorganized company. This right of conversion to expire two years after the consummation of the reorganization.

[fol. 667] Consolidation shall only be effective if two-thirds of the holders of Salt Lake Income Bonds voluntarily accept this reduction of interest from 6% to 4%, any non-assenting bonds to be called for payment or refunding at the convenience of the reorganized company. Unless such consents are obtained, no actual consolidation shall be consummated, and the reorganized company would simply affirm the tunnel lease and the present trackage agreements.

It will be observed that the fixed interest charges on the forty-one odd million dollars of first mortgage bonds amount to $1,233,604.00, which is slightly in excess of the figure arrived at by the application of the so-called Eastman formula (Opinion of Dec. 6, 1940, p. 7); which is justified if we capitalize the $15,000,000.00 that has been put back into the system since the ICC Plan was promulgated, more than half of which has been spent on that part of the system covered by the two Western divisional mortgages.

The contingent interest, 1% on the first mortgage bonds, and $1,363,025.00 on the income bonds, and three small amounts (See Notes 19 and 20), amounts to $1,853,212.00, which will be reduced by saving in interest in event of conversion of income bonds by the Reconstruction Finance Corporation into Class B stock as provided for. The prior charges on income, consisting of the Capital Fund, equipment trusts, divisional mortgage bonds and fixed and contingent interest charges, and sinking fund of one-fourth of [fol. 668] 1% on the income bonds, amounting to a grand total of all charges of $4,569,644.00, was earned in 1940.

This plan meets the principal objections of the creditors, especially the Insurance Group. It fully recognizes their first lien position, and, further, avoids any thinning, as charged, of the Rio Grande Mortgage to provide for cash payment of the Salt Lake bonds. It gives the Reconstruc-

tion Finance Corporation a means of liquidating the new money required from it, and, in addition, its current obligations of its temporary advances which were a poor risk when made. Except as stated this capital structure is well within the limits of the Interstate Commerce Commission Plan, thought to be necessary for reasons heretofore stated by the Court. It ranks the creditor's claims according to their legal priorities, which is all that can be asked for, and whether the creditors get any return or not will depend directly upon proper management of the property, and not upon the particular type of security the respective creditors get.

I again emphasize the provision for the earmarking and setting aside of the $750,000.00 a year Capital Fund. This, as well as the provision for setting aside and earmarking in a special fund the annual depreciation charge (Opinion of Dec. 6, 1940), are the best guarantees that can be put into the plan to assure the proper upkeep and maintenance of the property, the lack of which has always characterized the management of this system when in the hands of its [fol. 669] owners, and eliminates any temptation of future management "to bleed the adequate upkeep of the property in order to pay interest or dividends—a temptation that past managements have been unable to resist."

The Court again emphasizes its views (page 29 Opinion of Dec. 6, 1940) in respect to modification of the ICC provisions for the Reorganization Committee, being strongly of the opinion that the property should be under the direct control of the Court until the reorganization ~~plan is~~ completed. Further, it is suggested, in view of the small amount of bonds of any one issue represented by the Insurance Group, that their representation on the committee be cut to one member, and that the Court or some other proper authority name a member to represent the public interests of the citizens of Colorado.

The Court is of the opinion that the future of this property will be better assured if it is maintained as an independent unit and the control be not sold to any connecting carrier. These carriers are more dependent upon the Rio Grande than it is upon them. Artificial traffic control through stock ownership is restrictive in nature and tends to limit the value of the public service which the new company can render, as well as weaken the value of its secur-

ities, for "Freight traffic gravitates to the fastest schedule as quickly as water seeks its own level."

Even with the above modifications of the Interstate Commerce Commission plan in favor of the main line underlying Divisional Mortgages at the expense of the Recon- [fol. 670] struction Finance Corporation, it may be argued that the plan as modified is still too favorable to the Reconstruction Finance Corporation. The Court does not concur in this view. The security held by the Reconstruction Finance Corporation, namely, the Denver Gateway, is absolutely essential if the property is to have a future.

Transcontinental traffic, for which competition is so keen with the railroads to the north and south, must be held and built up if this debtor is to secure and hold the minimum traffic necessary to even maintain operating expenses and build up future interest requirements and dividends. The Trustees have demonstrated this can be done.

The Reconstruction Finance Corporation is in the better position to protect itself under an independent operation, and consideration must be given to the fact that it is asked to supply the new money necessary to make any plan effective and their reasonable requirements must be met if they do put up the new funds.

My three opinions in this matter, it is thought, set forth the reasons moving the Court to disapprove the ICC Plan and send it back to the Commission for further hearings and consideration. The Court recognizes the Commission is well versed and peculiarly fitted to appraise the values of different interests and the soundness and fairness of any plan. If it does not agree with the views of this Court, any new plan they submit is most likely to receive our approval. [fol. 671] The rights of the parties have been so minutely explored and discussed that it is hoped there may be little difficulty in the parties reaching an agreement upon a plan that meets the views of the Commission and the Court which are now in the record.

J. Foster Symes, District Judge.

Denver, Colorado, March 6, 1941.

Filed Mar. 7, 1941. George A. H. Fraser, Clerk.

(Here follows 1 paster, side folios 672-673)

[fols. 672-673]

EXHIBIT "A"

The Denver and Rio Grande Western Railroad Company Reorganization Plan of March 1, 1941

Distribution of New Securities as of January 1, 1941

Present Liabilities	Principal Amount[1]	Accrued Interest	Total[1]	Cash[2]	Undisturbed or Extended	50 Yr. 1st Mtg. Bonds (3% Fixed 1% Contingent Fully cumulative & to be paid before any interest on Income Bonds)[3] (Note A)	Percentages of Settlement of Claims of Divisional Mortgages: Principal (Note B)	Principal and Interest	75 Yr. Income 4½% Bonds Series A Non-cumulative Interest must be paid if earned up to 75% of net income to nearest ¼%, otherwise becomes cumulative	Percent of Principal & Interest	Preferred Stock 5%	Percent of Principal & Interest	Class A Common (No Par at $100 Beneficial interests to be distributed. Exchangeable for stock after 5 years and upon expiration of voting trust (Note 4)
Trustees' Certificates	$5,000,000		$5,000,000	(5)					$5,000,000[6]				
Reorganization Expense	1,000,000		1,000,000	(5)					1,000,000[6]				
Equipment Trusts[7]	5,789,000		5,789,000		$5,789,000[7]								
Rio Grande Western 1st Trust 4's	15,190,000	$3,645,600	18,835,600			$15,190,000	100.00%	80.65%	3,645,600	19.35%			
Rio Grande Western 1st Cons. 4's	15,080,000	3,770,000	18,850,000								$18,850,000	100.00%	
Rio Grande Junction Bonds, 5%	2,000,000	558,333	2,558,333			2,024,769	101.24	79.14	533,564	20.86			
D&RG 1st Cons. 4's and 4½'s	40,507,000	10,739,235	51,246,235			14,465,265	35.71	28.23	8,238,252	16.08	10,665,570	20.81	$17,877,148[8]
D&RGW Ref. and Imp. 5's and 6's	14,000,000	4,500,000	18,500,000			5,127,255	36.62	27.71	2,920,004	15.78	3,780,370[8]	20.44	6,672,371[8]
D&RGW Gen. Mortgage 5's	29,808,000	10,681,200[8]	40,489,200										13,355,381[8]
RFC Notes	10,691,850	2,161,934	12,853,784			4,312,853[9]	40.34	33.55	8,540,931[5]	66.45			
D&SL 1st Mortgage 4's	1,500,000		1,500,000		(1,500,000)[11]								
D&SL Income 6's[10]	9,734,000		9,734,000		(9,734,000)[11]								
Chase National Bank Loan[12]	1,500,000	478,458	1,978,458		(1,978,458)[13]	(14)			(14)		(14)		(14)
Railroad Credit Corp. Loan[15]	206,291		206,291[15]	$206,291[16]									
Denver and Salt Lake Minority Stock	4,111 shares		411,100						411,100				
Total			$188,952,001	$206,291[16]	$5,789,000	$41,120,142			$30,289,451		$33,295,940		$37,904,900[8]
Prior charges on income:													
Capital Fund (to take precedence over fixed interest)					$750,000(a)								
Equipment Trust Interest					138,076								
					$888,076								
Fixed and assumed interest:													
First Mortgage Bonds						$1,300,116[18]							
D&SL Divisionals. Interest but not principal assumed						449,360[17](b)							
						$1,749,476(c)							
Prior contingent interest:													
First Mortgage Bonds						433,372[19]							
						$2,182,848(d)							
Second contingent interest:													
Income 4½'s (Interest)									$1,419,840[20]				
Income 4½'s Sinking Fund									78,800[21]				
									$1,498,720				
Cumulative Capital Fund Fixed and Contingent Interest and Sinking Fund i. e., $888,076 + $1,749,476 + $433,372 + $1,419,840 + $78,880									$4,569,644(e)				

(a) Maximum.
(b) Earned and paid on D&SL First and Income Bonds in
(c) Earned 218 times in 1940.
(d) Earned 1¾ times in 1940.
(e) Earned in 1940.

Note A. Exactly the same proportionate allocation to divisions as provided in ICC Plan, after making provision for RFC "Cutoff" notes secured by Denver and Salt Lake Western stock.

B. Percentages of settlement of claims differ slightly from those shown on ICC Plan, due to change in effective date of Plan and various rates of interest accrual on divisional mortgage bonds.

1. Excluding pledged bonds.
2. Treasury cash not to be depleted (other than as provided in Note 16).
3. Absolute prior lien on existing D&RGW System (including Cutoff built by D&SLW) not shared by holders of D&SL liens.
4. Held in voting control pending forfeiture of conversion rights of RFC and cancellation of Class B Common, and for such further period as Court may fix to assure satisfactory management for stabilizing period; during which Voting Trustees upon prior approval of 2/3 of holders of beneficial interests with same limitation as to sale of over 40% to any one purchaser. (See Note 6).
5. To be obtained from proceeds of sale of 4½% Income Bonds to RFC.
6. RFC to purchase $6,000,000 of 4½% Income Bonds for cash, in addition to receiving $8,540,931 on old note advances. Total $14,540,931. Not less than $6,000,000, par value, of these bonds held by RFC to be convertible as a unit into Common Stock carrying sole voting power. Any sum realized by sale of Class B Stock or any part thereof to be applied first to reimburse the RFC for par value of such bonds so converted, and second to payment at par for cancellation of other

independently as it now does, shows continuous deficits for the stock since 1931, except in 1935 after fixed charges and [fol. 683] 6 percent interest on the income bonds.

The Commission should not in this case accord sole consideration to the severance study as a basis for fixing the value of the cut-off to the system. The statements of the Commission in the reorganization of the *Chicago & N. W. Ry. Co.*, in 236 I. C. C. 575, 239 I. C. C. 615, and of the United States District Court in *In Re Chicago and North Western Ry. Co.*, 35 Fed. Supp. 230, 240, referred to by the group as authority for relying solely upon the severance study for evaluating a bridge line, are not applicable where, as here, the bridge line affords by far the most direct access to one of the principal Eastern gateways of the property. Retention of control of the line is admittedly of prime importance to the debtor, and the past earnings of the line may be expected to be exceeded in the future.

The importance of the cut-off route to the system, and of access to the Denver gateway, are acknowledged by the parties, especially as affecting the ability of the system to compete with other trans-continental routes. The evidence of the increase of traffic interchanged with the Chicago, Burlington & Quincy Railroad at Denver as compared with the increase of interchange with the Missouri Pacific Railroad at Pueblo, Colo., since 1937, refutes the averment that the traffic position of the cut-off route has been stabilized. Continued development of traffic over the cut-off should serve to increase the importance and value of the cut-off, even on a severance basis.

The final position of the insurance group committee, in the light of the whole record, is seen in its acceptance of the court's provision for the Finance Corporation's claim. The group goes so far as to contend that this judicial deter- [fol. 684] mination is now the law of the case and as such controls all further proceedings before the Commission. The final position of the Finance Corporation consists substantially in the rejection of the court plan, a plea for recognition of the importance of the cut-off lines, and a request that the treatment of its notes shall be no less favorable than that accorded to the western divisional mortgages.

The court plan provided for the issue of new bonds in settlement of the Finance Corporation claim (as of Janu-

Percent of Principal & Interest	Preferred Stock 5%	Percent of Principal & Interest	Class A Common (No Par at $100) Beneficial interests to be distributed. Exchangeable for stock after 5 years and upon expiration of voting trust. (Note 4)	Percent of Principal & Interest	Class B Common (See Note 22)
19.35%					
	$18,850,000	100.00%			Proportion of Common A Issued
20.86					
16.08	10,665,570	20.81	$17,877,148[a]	34.88%	47.2%
15.78	3,780,370	20.44	6,672,371[4]	36.07	17.6
			13,355,381[4]	32.99	35.2
66.45					Of interest only if Common A finally acquires voting power
	(14)		(14)		
	$33,295,940		$37,904,900[4]		

) Maximum.
) Earned and paid on D&SL First and Income Bonds in 1940.
) Earned 218 times in 1940.
) Earned 1¾ times in 1940.
) Earned in 1940.

nds.

ient for stabilizing period, during which Voting Trustees would have right of sale

se bonds held by RFC to be convertible as a unit into total issue of Class B Com- and second to payment at par for cancellation of other Income Bonds then held that no one purchaser can obtain more than 40% thereof. Conversion privilege

mprovements.

holders of Income Bonds voluntarily consent (1) to a reduction of fixed interest of D&SL Divisional Bonds (i. e., either 1st 4's or Incomes except in refunding): ivisional mortgages undisturbed as to existing security and covering D&SL prop-

ary 1, 1941), on the basis of $4,312,853 in first-mortgage 50-year bonds and $8,540,931 in income-mortgage 75-year bonds. It is believed that the amount of first-mortgage bonds thus assigned was intended to represent the loan made for construction of the cut-off. According to the analysis made by counsel for the insurance group of the value of the Salt Lake stock and other pledged collateral, this treatment of the Finance Corporation was liberal; according to the counsel for the Finance Corporation it does not give proper recognition to the pledged collateral, especially to the element of control of the cut-off. The court's treatment of the Finance Corporation's claim clearly was influenced by the concurrent proposal that the Finance Corporation would take $6,000,000 of new income bonds at par, advancing the cash required to pay the $5,000,000 of trustees' certificates outstanding and $1,000,000 of reorganization expenses. No provision apparently was made for paying or refunding the Salt Lake income bonds, the owners of which do not assent to the proposed modification of interest terms. The amount of such nonassenting bonds might, as a maximum, be approximately $3,309,000.

If the matter of new financing be separately considered, [fol. 685] to be carried out through a direct loan to the new company, secured by an appropriate amount of new securities, or purchase of such securities, then the treatment of the Finance Corporation's existing notes might logically be based on the securities pledged, with appropriate provisions effective if consolidation with the Salt Lake is not effected through the means provided.

The securities pledged with the Finance Corporation which are of classes that are also outstanding in the hands of the public comprise $783,000 of D. & R. G. consolidated 4-percent bonds, $10,000 of R. G. Western first-trust 4-percent bonds, $1,395,000 of R. G. Western consolidated 4-percent bonds, $4,385,000 of refunding and improvement mortgage 5-percent bonds, and $1,266,000 of Salt Lake income bonds. Under the plan recommended herein, the holders of these securities would be entitled to receive the following securities of the new company: $2,305,300 of first-mortgage bonds, $1,386,650 of income bonds, $2,079,850, par value, of preferred stock, and 20,672 shares of common stock.

The so-called outside securities under pledge are the $1,777,000 of Rio Grande Southern first-mortgage 4-percent

Equipment (First Division)		188,076	
		$888,076	
Fixed and assumed interest:			
First Mortgage Bonds		$1,300,116[18]	
D&SL Divisionals. Interest but not principal assumed		449,360[17](b)	
		$1,749,476(c)	
Prior contingent interest:			
First Mortgage Bonds		433,372[19]	
		$2,182,848(d)	
Second contingent interest:			
Income 4½'s (Interest)			$1,419,840[20]
Income 4½'s Sinking Fund			78,800[21]
			$1,498,720
Cumulative Capital Fund Fixed and Contingent Interest and Sinking Fund i. e., $888,076 + $1,749,476 + $433,372 + $1,419,840 + $78,880			$4,369,644(e)

(b) Earned 218 times in 1940.
(d) Earned 1¾ times in 1940.
(e) Earned in 1940.

Note A. Exactly the same proportionate allocation to divisions as provided in ICC Plan, after making provision for RFC "Cutoff" notes secured by Denver and Salt Lake Western stock.

B. Percentages of settlement of claims differ slightly from those shown on ICC Plan, due to change in effective date of Plan and various rates of interest accrual on divisional mortgage bonds.

1. Excluding pledged bonds.
2. Treasury cash not to be depleted (other than as provided in Note 16).
3. Absolute prior lien on existing D&RGW System (including Cutoff built by D&SLW) not shared by holders of D&SL liens.
4. Held in voting control pending forfeiture of conversion rights of RFC and cancellation of Class B Common, and for such further period as Court may fix to assure satisfactory management for stabilizing period, during which Voting Trustees upon prior approval of 2/3 of holders of beneficial interests with same limitation as to sale of over 40% to any one purchaser. (See Note 6).
5. To be obtained from proceeds of sale of 4½% Income Bonds to RFC.
6. RFC to purchase $6,000,000 of 4½% Income Bonds for cash, in addition to receiving $8,540,931 on old note advances. Total $14,540,931. Not less than $6,000,000, par value, of these bonds held by RFC to be convertible as a unit into to mon Stock carrying sole voting power. Any sum realized by sale of Class B Stock or any part thereof to be applied first, to reimburse the RFC for par value of such bonds so converted; and second to payment at par for cancellation of other by RFC out of holdings received in reorganization, and any remainder paid into the sinking fund provided for 1st Mortgage Bonds. Right of sale of this stock by RFC to be restricted so that no one purchaser can obtain more than 40% there to expire 2 years after consummation of reorganization.
7. Including Equipment Trust, Series G, $1,260,000, issued February 1, 1941.
8. Excluding $7,452,000 of contingent interest accrued in five year period ended February 1, 1929, and excluding 50% payment which was made on coupon due February 1, 1934.
9. RFC "Cutoff" notes secured by D&SLW stock. D&SLW has no indebtedness and stock represents unencumbered ownership of Cutoff mileage, of increased value account subsequent improvements.
10. Excluding $1,266,000 principal amount, pledged with RFC, to be cancelled.
11. Under terms of D&SL Income Bonds they become a fixed obligation as to interest at 6% as and when any consolidation is effected. Consolidation shall only be effected if 66-2/3% of holders of Income Bonds voluntarily consent (1) to a r from 6% to 4% and (2) to the call for payment or for refunding (at the convenience of the reorganized company) of Income Bonds not consenting. No further issuance or negotiation of D&SL Divisional Bonds (i. e., either 1st 4's or Inco Not to be assumed as to principal by reorganized company, but interest at 4% on 1st 4's and on the Incomes to be assumed for present life of bonds. Status of 1st 4's and Incomes: divisional mortgages undisturbed as to existing security a erties, full right reserved to refund without assumption. Tunnel contract to be assumed by reorganized company. Unless such consents are obtained, no actual consolidation would be in effect; in that event the balance of the Plan would no no provision would be necessary for minority holders of Salt Lake stock. The reorganized company would then own free in its treasury the Salt Lake stock now pledged to RFC; there would then be no assumption of interest on the Salt Lake the trackage agreement would remain in effect.
12. Interest on Chase Bank note computed in accordance with claim of Bank at 6% from date petition filed under Sec. 77, as provided by laws of State of New York. Subject to final determination.
13. To be a 4% note secured by pledge of following for claim of $8,001,000 on pledged R. and L. 5's; New 1st's, $2,217,077; New Income 4½'s, $1,262,558; New 5% Preferred, $1,635,401; New Common A, $2,885,961.
14. Collateral to be pledged, as listed in Note 13, but not included in totals shown above as outstanding. Interest payable on such collateral is shown in summary of fixed and contingent interest above. Maximum interest payable annually (ex tions) limited to 4% on $1,978,458, or $79,138.32, with excess payments received as interest or dividends from collateral applied to reduction of principal of note.
15. In computing amount due Railroad Credit Corporation, the balance due D&RGW under Marshalling and Distributing Plan has been deducted.
16. To be paid from cash in Treasury upon consummation of Plan, and collateral due in reorganization cancelled.
17. Consists of Divisional Mortgage Bonds (unassumed as to principal): D&SL 1st 4's, $60,000; D&SL Incomes (100% exchanged or balance refunded), $389,360; Total, $449,360.
18. Consists of $1,233,604 fixed interest on $41,120,142 First Mtg. Bonds to be outstanding.
66,512 fixed interest on 2,217,077 First Mtg. Bonds to be pledged as collateral for Chase Note.

$1,300,116	$43,337,219

19. Consists of $ 411,201; 1% contingent interest on $41,120,142, First Mtg. Bonds to be outstanding.
12,602; balance of interest at 4% on Chase Bank note, the payment of which is contingent upon interest payments on new Firsts to be pledged as collateral for such note.
9,569; to be applied to reduction of principal of Chase Bank note when 1% contingent interest is paid on new Firsts to be pledged.

$ 433,372

20. Consists of a maximum of $1,363,025 interest on $30,289,451 Income 4½'s to be outstanding.
56,815 to be applied to reduction of principal of Chase Bank note if maximum interest of 4½% is paid on Income Mortgage Bonds.

$1,419,840—Will be affected by: 1. Interest limitation required by Chase Bank note (difference applicable to principal). 2. Interest ceasing on any conversion by RFC to Class B Common.

21. ¼ of 1 per cent of the following outstanding and pledged Series A Income Bonds: $30,289,451 outstanding Series A Income Bonds.
1,262,558 Series A Income Bonds pledged under Chase Bank note (applicable to principal).

$31,552,099

22. Class B Common (No Par Value): None to be issued unless RFC exercises its right of conversion, then 100,000 shares to be issued.

bonds, 500 shares of Goshen Valley stock, 73,710 shares of Denver-Colorado Springs-Pueblo Motor Way stock, and 1,564 shares of Rio Grande Motor Way stock. The only one of these items for which any realizeable value is claimed by the Finance Corporation is the Denver-Colorado Springs-Pueblo Motor Way stock, which is said to have a cash value in excess of $200,000. In respect of these outside securities it would be appropriate for the Finance Corporation to receive a note in the amount of $250,000 secured by the securities mentioned.

[fol. 686] The original cost of the Dotsero cut-off is represented approximately by the 36,310 shares of capital stock, taken at $100 a share. The Salt Lake Western has no funded debt. Viewed as a construction project, the financing in such a case might be assumed to be by means of stock and bonds in equal proportions. For the Salt Lake Western stock held by the Finance Corporation, comprising all of such stock outstanding, it would be reasonable to assign $1,815,500 of new first-mortgage bonds, 9,077 shares of new preferred stock, and 9,078 shares of new common stock. While the earnings of the Salt Lake Western are not available separately, the foregoing amount of new bonds assigned is not excessive in relation to the rental under the lease.

As to the stock of the Salt Lake held by the Finance Corporation, the record justifies the conclusion, and the Commission should so find, that the future of the reorganized system will depend upon maintaining control of the Denver gateway through the cut-off route, and that control of this route by the Finance Corporation through its stockholdings of the Salt Lake and the secondary debtor constitutes an asset which should be recognized in the reorganization. But, disregarding this asset in the present analysis, and on the showing as to the value of the cut-off to the system solely from an earning standpoint, it would seem improper to recognize the Salt Lake stock through an allocation of new bonds. The circumstances, however, clearly justify assigning on this basis shares of new common stock of the reorganized company in an amount equal to the shares of Salt Lake stock held by the Finance Corporation.

On the basis of the foregoing study regarding the collateral pledged with the Finance Corporation the total new securities which would be issuable are $4,120,800 of new

first-mortgage bonds; $1,386,650 of new income bonds; [fol. 687] 29,876 shares of new preferred stock; 75,639 shares of new common stock, and a promissory note for $250,000.

It is clear that the foregoing allotment of securities does not adequately reflect the value of control of the cut-off held by the Finance Corporation through the pledge with it of practically all the stock of the properties. The above-stated securities may represent those which it is entitled to receive and hold regardless of the element of control. But the strategic position of the cut-off, its access to the principal Eastern gateway, and the situation as one leg of the wye which constitutes the system, justify the conclusion that the allocations shown in the study should be modified to give the Finance Corporation substantially better treatment. It is recommended that the claim be treated as well as the R. G. Western first-trust bonds or the Junction bonds. As hereinafter indicated these bonds, under the recommended plan, will receive new first-mortgage bonds in respect of 57 percent of the claim and new income bonds in respect of 43 percent of the claim. Accordingly, it is recommended that $7,570,431 of new first-mortgage bonds and $5,711,027 of new income-mortgage bonds be allocated to the Finance Corporation's claim. The recommended treatment of the claim in the event that the consolidation with the Salt Lake is not effected, is indicated below.

Denver and Salt Lake income bonds

Under the terms of the Salt Lake income mortgage, interest becomes fixed at 6 percent if consolidation with another road is effected. During the 10-year period 1931-40 the earnings of the Salt Lake available for interest averaged 4.34 percent per annum on the amount of income bonds outstanding and the average payment was 4.2 percent. [fol. 688] From 1928 to 1931, and in 1935, 6 percent was paid. The available income during the 10-year period averaged $478,000. This sum approximates the annual income indicated by the severance study, hereinbefore mentioned, as representing the contributive value of the cut-off to the system. In line with the evidence and the conclusion stated above with respect to the value of the cut-off to the system, the plan should provide, in connection with the consolidation, for modification of the interest terms of

$33,295,940	$37,904,909[1]

) Maximum.
) Earned and paid on D&SL First and Income Bonds in 1940.
) Earned 218 times in 1940.
) Earned 1¾ times in 1940.
) Earned in 1940.

nds.

ient for stabilizing period, during which Voting Trustees would have right of sale

se bonds held by RFC to be convertible as a unit into total issue of Class B Com-
, and second to payment at par for cancellation of other Income Bonds then held
that no one purchaser can obtain more than 40% thereof. Conversion privilege

mprovements.

f holders of Income Bonds voluntarily consent (1) to a reduction of fixed interest
of D&SL Divisional Bonds (i. e., either 1st 4's or Incomes except in refunding).
ivisional mortgages undisturbed as to existing security and covering D&SL prop-
in effect; in that event the balance of the Plan would not be affected except that
would then be no assumption of interest on the Salt Lake issues. In either event,

letermination.
New Common A, $2,885,961.
nterest above. Maximum interest payable annually (except in case of accumula-

e.

on by RFC to Class B Common.

the trustees, their counsel, and technical adviser. It would [fol. 691] appear that the Commission's estimate of $1,000,000 for total reorganization expenses no longer applies, and that such of these costs as now remain may possibly be defrayed by the use of the debtor's cash without impairing working capital.

For the new money required in the reorganization, other than for reorganization expenses, the plan should provide for a 12-year loan either by the Finance Corporation or through private channels in the amount of $5,000,000 for the payment of trustees' certificates outstanding, and in the event that consolidation of the Salt Lake is effected for such additional amount as may be necessary in connection with the payment, purchase, or refunding of the Salt Lake income bonds the holders of which do not assent to the proposal regarding these bonds. As collateral security for this loan, there should be issued by the new company, for pledge with the lender, first-mortgage bonds in an amount equal to 125 percent of the amount of the loan, or such other amount as shall be required by the lender and approved by the Commission. As an alternative to such a loan, the plan should provide that not exceeding $10,000,000 of new first-mortgage bonds may be issuable for sale to provide the new money required, as may be determined by the reorganization committee and approved by the court and the Commission.

Earnings; equity

In its report 233 I. C. C. 515, *supra*, at pages 551-2, the Commission discussed the earnings record of the carriers, and showed that the lowest system income available for interest in the last decade was in the 3-year period 1936-38. After adjustment for extraordinary expenditures for deferred maintenance, the average annual income available was stated at about $2,893,255. The total of the fixed-interest charges approved and the maximum annual pay-[fol. 692] ment to the capital fund was approximately $2,098,536, which would be covered 1.38 times by the foregoing amount of adjusted income.' The Commission there said

> In giving this consideration to the low earnings of recent years our position is not that the system lines will never regain their former earning power, or ex-

[fol. 674] INTERSTATE COMMERCE COMMISSION

Washington

Finance Docket No. 11902

Denver & Rio Grande Western Railroad Company
Reorganization

SUMMARY OF PROPOSED REPORT

This report contains the examiner's recommendations for a revision of the modified plan of reorganization of The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor, approved by the Commission on April 2, 1940, 239 I. C. C. 583. The evidential basis for the report includes the record made in the court proceedings following the certification of the modified plan to the court, and the further hearing held by the Commission on May 20, 1941.

Under the recommended plan, effective date January 1, 1942, the capitalization of the new company, on the basis of a consolidation of all the affiliated companies, including The Denver and Salt Lake Railway Company, would be as shown in appendix A of the report, and is summarized as follows:

Equipment obligations, undisturbed	$8,254,825
Chase Nat. Bank note, extended	2,068,458
R.R. Credit Corp. note, extended	268,953
Loan for new money, approximately	6,000,000
New first-mortgage bonds	34,579,366
New income bonds	34,925,295
D. & Salt Lake first-mtge. bonds	1,500,000
D. & Salt Lake income bonds, modified	9,734,000
Total debt	97,330,897
New preferred stock	29,013,585
New no-par common stock, taken at $100 a share	42,840,570
Total	169,185,052

ceed it, but rather that with the present conditions in the railroad field and in the public interest, a conservative policy should be followed * * *.

The evidence adduced at the further hearing shows that the improvement program has been substantially completed. From the appointment of the debtor's trustees on November 1, 1935, to March 31, 1941, a total of $22,916,051 was expended on the debtor's property, of which $17,504,246 was chargeable to capital account. The ratio of maintenance to total revenues had been 35.12 in 1935, 41.09 in 1936, 46.83 in 1937, and 39.09 in 1938. The debtor believes that the improvements already made, together with the coming acquisition of new Diesel switch engines and road engines costing $4,000,000, will produce a large and permanent reduction in operating costs. The results of operation in 1940 are considered by the insurance group committee to be fairly representative as to economy of operation as well as to gross revenue, based on five years of the trusteeship. The income of the Denver available for interest in 1940 was shown as $2,800,514* and the Salt Lake's available income as $509,771, a total of $3,310,285. Applying the unit costs of operation in 1940, the available income of the combined roads would have been $3,288,591 [fol. 693] in 1939, $2,970,135 in 1938, $3,774,334 in 1937, and $3,890,570 in 1936. The average for the five years is $3,446,765. These figures reflect operating charges of approximately $1,000,000 a year in connection with improvements. The forecast for 1941 shows an available income of $3,513,590 for the combined roads.

These figures indicate an improvement in the earning power of the system but do not justify a reconsideration of the Commission's findings regarding the equity of the Denver's stockholders (233 I. C. C. 515, at page 580) or of the holders of unsecured claims (239 I. C. C. 583, at page 594). The Commission pointed out that the annual interest charges on the debt of the Denver as of June 30, 1938, amounted to $5,919,227 and the charges on the debt of the system amounted to $6,563,267. Between June 30, 1938, and January 1, 1942, the increase in debt, due to interest accruals and new equipment obligations, will exceed

*Adjusted from the amount $2,647,086 shown in the 1940 annual report of the Denver's trustees to the stockholders.

[fol. 675] Based on this capital structure the annual charges would be substantially as follows:

	Fixed	Prior Contingent	Contingent	Preferred Dividends
Equipment obligations	$195,000			
Chase Bank note	49,835	$16,612	$16,150	
R.C.C. note	2,690			
Loan for new money, approx.	240,000			
New first mtge. bonds	1,037,381	345,794		
D. & S. L. first mtge. bonds	60,000			
D. & S. L. income bonds	389,360	194,680		
New income bonds			1,571,638	
Preferred stock				$1,450,679
Totals	1,974,226	557,086	1,587,788	1,450,679
Capital fund, maximum payment			750,000	
Sinking fund for first mtge. bonds			172,897	
Sinking fund for income mtge. bonds			87,313	

Under this plan the Denver & Salt Lake would be consolidated with the debtor only in the event the holders of at least 66⅔ per cent of the Denver & Salt Lake income bonds voluntarily accept an extension of the maturity date of the bonds to that of the first-mortgage bonds issued by the new company, and to a modification of interest on the Denver & Salt Lake income bonds to provide for 4 percent fixed interest and 2 percent contingent interest.

The proposed allocation of new securities to each class of claims is shown on appendix A. The holders of bonds of the classes shown below would receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, the following amounts of new securities:

Rio Grande Western Railway Company first-trust bonds, $728.77 of new first-mortgage bonds and $551.23 of new in-
[fol. 676] come bonds; Rio Grande Western Railway Company consolidated mortgage bonds, $322.50 of new income bonds and $967.50, par value, of new preferred stock; Junction first-mortgage bonds, $757.53 of new first-mortgage bonds and $571.54 of new income bonds; Denver & Rio Grande Railroad Company consolidated mortgage 4-percent bonds, $260.00 of new first-mortgage bonds, $260.00 of new income bonds, $260.00, par value, of new preferred stock, and 5.2 shares of new common stock; Denver & Rio Grande Railroad Company consolidated mortgage 4½ percent bonds, $267.50 of new first mortgage bonds, $267.50 of new income bonds, $267.50, par value, of new preferred stock,

and 5.35 shares of new common stock; the debtor's refunding and improvement 5-percent bonds, $272.50 of new first mortgage bonds, $272.50 of new income bonds, $272.50, par value, of new preferred stock, and 5.45 shares of new common stock; the debtor's refunding and improvement 6-percent bonds, $287.00 of new first-mortgage bonds, $287.00 of new income bonds, $287.00, par value, of new preferred stock, and 5.74 shares of new common stock; the debtor's general mortgage bonds, 4.69 shares of new common stock.

The Reconstruction Finance Corporation would be entitled to receive, in full settlement of its notes, new first-mortgage bonds equal to 57 percent of the claim and new income bonds equal to 43 percent.

(Here follows topical index to report which is not reproduced herein.)

[fol. 677] INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

Denver & Rio Grande Western Railroad Company Reorganization

Submitted — *Decided*

Upon record previously made in the proceedings before the court and the Commission, and upon further hearing before the Commission, a revised plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, recommended.[1]

Appearances as in prior reports, and also *Montgomery Dorsey*, *William J. Kane*, and *Emmet McCaffery*.

REPORT PROPOSED BY M. S. JAMESON, EXAMINER

By its report and order of April 2, 1940, in this proceeding, 239 I. C. C. 583, the Commission approved a modi-

[1] Previous reports: 212 I. C. C. 105 and 709; 217 I. C. C. 101; 224 I. C. C. 574; 233 I. C. C. 515; 242 I. C. C. 629 and 721.

fied plan of reorganization of The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor. The modified plan was duly certified to the District Court of the United States for the District of Colorado, where proceedings for reorganization of the above-named companies are pending. Pursuant to an order of the court entered May 6, 1940, objections to the plan were filed with the court by the debtor, the insurance group committee, the Finance Corporation, and other parties, and the case [fol. 678] came on for hearing on July 29, 1940. Following an informal conference with the parties after the close of the hearing, the judge issued an interim memorandum, dated August 30, 1940, in which he expressed his views regarding the main features of the plan. Further conferences were held and a new plan, proposed by the insurance group committee and known as the discussion plan, was considered. On December 6, 1940, the judge filed an opinion in which he criticized the discussion plan and the Commission plan, and suggested a different plan.

The abbreviated titles of companies used in the Commission's reports will be followed herein.

The adoption of the discussion plan was urged in a petition filed with the court by the Central Hanover Bank & Trust Company, trustee of the R. G. Western first-trust mortgage. On January 6-8, 1941, the court heard the parties in oral argument, after which several conferences were held. A plan referred to as the FitzGibbon plan was presented at these conferences. On March 7, 1941, the court entered an order overruling a motion to dismiss the proceedings, disapproving the Commission plan, and referring the proceedings back to the Commission with an opinion dated March 6, 1941. In this opinion the judge indicated his objections to the various plans offered, including the Commission plan and a plan proposed by the Finance Corporation, and described a plan which he recommends. This plan will be referred to hereinafter as the court plan. The record made in the court proceedings was transmitted to the Commission.

Upon petition by the insurance group committee an order was entered reopening the proceeding and assigning it for further hearing on May 20, 1941, for the purpose of receiving evidence to bring the record of the debtor's opera- [fol. 679] tions down to date, and such other evidence and

suggestions as would assist in a reconsideration of the approved plan. Briefs were filed. The briefs were devoted largely to criticisms of, and suggested changes in, the court plan.

The court plan differs in essential respects from the Commission's modified plan although intended to be within the framework of the latter. The court agrees with the Commission regarding a consolidation of the lines, stating in its opinion that, "Considering the public's point of view and that of all creditors, this particular situation requires a consolidation of the Rio Grande and the Denver & Salt Lake." But under the court plan the consolidation would be effected only in the event the holders of at least 66⅔ percent of the Salt Lake income bonds voluntarily accept a modification of the interest provisions of these bonds so that they would bear fixed interest at 4 percent and contingent interest at 2 percent per annum. The effective date of the court plan is January 1, 1941, while that of the Commission plan is June 30, 1938, involving an increase of approximately $15,000,000 in accrued interest on funded debt, together with new equipment obligations. The amount of new first-mortgage bonds was increased from $29,403,144 of 4-percent bonds in the Commission's plan to $41,120,142 of bonds bearing 3-percent fixed interest and 1-percent prior-contingent interest. The $1,278,539 of annual fixed charges in the Commission plan was increased to $1,887,552 in the court plan, principally by the inclusion of the Salt Lake bonds. The distribution of securities allocated to others than the Finance Corporation was generally on the basis of the Commission plan, but, due to the increase in first-mortgage bonds and the different treatment of the claims of the Finance Corporation, the treatment of the Denver's bonds [fol. 680] was much more favorable than in the Commission plan. The court plan provides that the payment to the capital fund, a maximum of $750,000 per annum, be made prior to the payment of fixed interest, rather than immediately following. For the new money required in the reorganization the Finance Corporation would purchase $6,000,000 of income bonds which would be convertible as a unit into class-B common stock, carrying sole voting power. The right of sale of this stock by the Finance Corporation, for its reimbursement, would be restricted so that no one purchaser could obtain more than 40 percent thereof. These matters, the suggestions made by the

various parties, and the evidence presented since the record before the Commission was previously closed (December 1, 1939), are discussed below.

In its report, 239 I. C. C. 583, *supra*, the Commission reviewed the development of the cut-off route, the close affiliation between the component roads, the Moffat tunnel interest, and the question of public interest, and reaffirmed its previous finding that the properties should be consolidated in connection with this reorganization. The Commission also pointed out the status of the Finance Corporation as pledgee of the stocks of the Salt Lake and Salt Lake Western, and stated its reasons for the treatment accorded the claims of the Finance Corporation in the plan. It appears that the court rejected the Commission's plan because, through this treatment of the Finance Corporation and the relative treatment of the debtor's bondholders, particularly those owning the bonds of the R. G. Western and the Junction, the price to be paid for consolidation was too high, and the plan was deemed inequitable. It is apparent that the Commission plan must be disregarded as being impossible of approval or acceptance and that a new plan [fol. 681] should be prepared on the general basis of the court's plan for consolidation with the Salt Lake.

Provisions for consolidation

Both classes of Salt Lake bonds should retain their present lien whether or not the consolidation is effected; in the event of consolidation the bonds of the new company should be secured by the combined properties of the debtor, the secondary debtor, the Junction, and the Goshen Valley; otherwise by those of the debtor, the Junction, and the Goshen Valley. The merger or consolidation of these properties, together with the Salt Lake, should be undertaken, and if the proposal is accepted by the holders of the required percent of income bonds, as hereinafter described, should be effected in a manner to be determined by the reorganization committee, subject to approval by the Commission and the court, and under a fair and equitable arrangement to protect the interests of the railroad employees affected, as required by law. The new plan should indicate the treatment of the various claims on the basis of such a consolidation, and also on the basis of continued separate operation of the Salt Lake, in which case the Salt Lake

bonds and the stock outstanding in the hands of the public would remain undisturbed. In the event that the consolidation with the Salt Lake is effected, the tunnel contract would be assumed by the new company.

Finance Corporation claims

The notes held by the Finance Corporation, with interest accrued to December 31, 1941, constitute a total claim of approximately $13,281,458, after certain credits for interest on pledged bonds and a payment of $700,000 on the loan in connection with a rescission of the sale of 3,651 shares of Salt Lake Stock to the debtor. The collateral [fol. 682] securing the indebtedness to the Finance Corporation consists of the bonds, stocks, etc., enumerated in the Commissions' report, 233 I. C. C. 515, at page 524, except for changes in the amounts of Salt Lake and motor companies' stocks, the amounts of these securities on pledge now being Salt Lake stock, 45,889 shares, Denver-Colorado Springs-Pueblo Motor Way, 73,710 shares, and Rio Grande Motor Way, 1,564 shares.

In support of their contention that the stock of the Salt Lake and Salt Lake Western is without value, counsel for the insurance group rely on the severance study which they introduced at the court hearing, and the record of the Salt Lake's earnings. The severance study, severely criticized by the Finance Corporation, purported to show that for the year 1939, on the most favorable basis of computation for the Salt Lake, the Denver's income available for interest would have been increased by $323,451 if the Salt Lake and Salt Lake Western had been operated as a single independent road, interchanging traffic with the Denver at Dotsero; that the Denver had lost money by the cut-off operation; that the $391,000 of income of the Salt Lake available for interest in 1939 would have been converted into a deficit of $182,229 by the severance; that if all the roads had been operated as a consolidated system in 1939 the income available for interest would have been $2,512,184, while with the cut-off lines divorced it would have been $2,064,368. Counsel concluded that something like $500,000 a year is the maximum realizable value of the Salt Lake-Salt Lake Western to the Denver, such sum being less than the annual interest on the Salt Lake bonds outstanding. The actual earnings' record of the Salt Lake operating

the Salt Lake income bonds to provide for 4 percent fixed interest and 2 percent contingent interest. Additional considerations in support of this modification are the desirability of accomplishing the consolidation with the Salt Lake, and the fact that it was determined by the court and incorporated in the court plan. It is recommended, accordingly, that the proposal submitted to the holders of the Salt Lake income bonds shall be that the interest provisions of the bonds be modified to 4 percent fixed interest and 2 percent prior contingent cumulative interest, payable on a parity with similar fixed interest and contingent interest on the new first-mortgage bonds, and that the maturity date of the bonds be extended to the maturity of the new first-mortgage bonds.

In the event that the holders of 66⅔ percent of the Salt Lake income bonds fail to accept the proposal for modification of the bonds, and the consolidation with the Salt Lake is not effected, the claims of the Finance Corporation should be provided for as follows: For the $783,000 of D. & R. G. consolidated mortgage 4's, $10,000 of Rio Grande Western first 4's, $1,395,000 of Rio Grande Western consolidated 4's, and $4,385,000 of the debtor's refunding and improvement 5's pledged as part security for the loans, the Finance Corporation should receive the following new securities: [fol. 689] $1,039,300 of new first-mortgage bonds, $1,386,650 of new income bonds, 20,799 shares of new preferred stock, and 20,672 shares of new common stock. The balance of the claim, if consolidation is not effected, should be covered by a 12-year note to the Finance Corporation secured by pledge of the Salt Lake income bonds, the Rio Grande Southern bonds, the motorway stocks, the Salt Lake stock, and the Salt Lake Western stock. It should be provided that the Finance Corporation would have all the rights of ownership in these stocks insofar as voting such stocks is concerned. The amount of the note should be $7,500,000 and it should bear fixed interest at the rate of 1½ percent and contingent interest at the rate of one-half of 1 percent per annum, representing the prospective return on the Salt Lake income bonds pledged, plus the return on the new first-mortgage bonds which were assignable to the Salt Lake Western stock under the treatment of the Finance Corporation's claim first described. In addition to the foregoing interest the Finance Corporation should be entitled to additional interest on the note to the extent of all interest and dividends

paid on the pledged collateral other than the Salt Lake income bonds and the Salt Lake Western stock, subject to the condition that the total interest paid on the note shall not exceed 4 percent per annum. The new company's obligation as to payment of interest, or principal and interest, of this note should be limited, respectively, to the proceeds of the sale of the pledged securities and the income from such securities, without recourse to the new company for any deficiency. The reorganized company should have the right, at any time, to redeem the collateral through payment of the principal of the notes and any unpaid interest payable under the terms of the notes.

[fol. 690] This provision for an alternate treatment of the Finance Corporation's claims necessarily eliminates the allotment of first-mortgage bonds and income bonds to the Finance Corporation indicated on appendix A.

New money requirements

Whether or not the consolidation with the Salt Lake is effected, new money will be required in the reorganization for the payment of trustees' certificates outstanding in the amount of $5,000,000, and possibly for other purposes, as indicated below. The judge disapproved the use of funds in the hands of the trustees for such purposes, urging that part of the cash on hand be used for the new locomotives, authorized by court order on February 10, 1941, and that an adequate cash balance be kept on hand. He stated in this connection that the trustees considered that they should have a working balance of not less than $1,250,000. At the further hearing the debtor's general auditor testified that $2,000,000 would be ample. The debtor's cash forecast shows $3,553,618 on hand at the beginning of 1941 and $3,027,941 at the close, after payments aggregating $1,422,811 for new equipment. The cash position evidently precludes the use of funds for the payment of trustees' certificates but it might permit payment of the expenses of reorganization now remaining. By its report of August 26, 1940, in this proceeding, 242 I. C. C. 629, division 4 fixed maximum limits of allowance for compensation and expenses of trust companies, committees, their counsel, etc., up to May 20, 1940, in the total amount of approximately $268,000. Previously, approximately $225,000 had been paid out of the debtor's estate, largely as compensation of

$24,000,000. It is plain that the situation as regards the equity has remained unchanged. The court has not suggested otherwise. The Commission should reaffirm its findings that the equities of the owners of the debtor's common stock and preferred stock have no value and that the holders of claims in classes 1 and 2 are not entitled to participate in the plan; and that the equity of the holders of unsecured claims not entitled to priority is without value and that these creditors should not be permitted to participate in the plan.

New capital structure

The effective date of the new plan should be January 1, 1942, and the amount of accrued interest to that date on fixed obligations should be added to the principal amounts of such obligations as the basis for the allocation of new [fol. 694] securities. The resulting totals are shown in the second column of appendix A.

In preparing its plan the court was in possession of the system earnings statements up to and including 1940. Notwithstanding the reference in the opinion of March 6, 1941, to the desirability of keeping fixed charges within the limit of those in the Commission's plan because of uncertainties as to taxes, labor costs, etc., the fixed charges in the court plan would be $1,887,552, or $2,637,552, including the maximum payment to the capital fund, which is placed ahead of all fixed interest. As pointed out in the brief of the Finance Corporation, there would be a further increase of $411,201 if the court plan were modified so as to make the prior contingent interest on the new first-mortgage bonds a fixed charge in the event all fixed and contingent interest should be earned 1½ times in each of three calendar years in any five consecutive years, such three years to include the last two of such five years. This modification was proposed by the insurance group committee. It should be rejected for the reason that adequate treatment would be afforded to those receiving the new first-mortgage bonds through the provision that the interest payment of 1 percent is to be prior to other contingent interest and fully cumulative.

On the basis of the present record the Commission should find that, after due consideration of the probable prospective earnings of the properties in the light of their earnings experience and other relative facts, there will be

adequate coverage of fixed charges of approximately $2,000,000 per annum by the probable earnings for the payment thereof, but that the fixed charges should not exceed that by any substantial amount. Payments into the capital fund should not be included as an item in the limiting amount.

[fol. 695] The new capital structure and the allocation of securities recommended are shown in tabulated form in appendix A, based on consolidation of the Salt Lake properties and a modification of the interest on the Salt Lake income bonds. Under this plan the fixed charges would approximate $1,974,266 per annum, comprising fixed interest at 3 percent on $34,579,366 of new first-mortgage bonds, at 4 percent on $1,500,000 of Salt Lake first mortgage bonds, and 4 percent on $9,734,000 of Salt Lake income bonds, together with the estimated fixed-interest charges on the Chase Bank note extended, the Railroad Credit Corporation note extended, the loan to provide new money, assumed at $6,000,000, and the equipment obligations outstanding. Prior contingent-interest charges on the new first-mortgage bonds, the Salt Lake income bonds, and the Chase Bank note would approximate $557,086 per annum. Contingent-interest charges on the $34,925,295 of new income bonds and the Chase Bank note would total $1,587,788. The total debt of the new company under this plan would be approximately $97,330,897, and the total capitalization, taking the no-par common stock at $100 a share, would be approximately $169,185,052. Of this total, the total debt will be approximately 57 percent. Total charges ahead of dividends on the preferred stock, including the maximum payment to the capital fund and the sinking funds for retirement of bonds, would be approximately $5,129,350 as compared with $4,093,842 in the Commission's modified plan. This increase is justified on the basis of the new evidence referred to above. The Commission should find that these amounts may not be exceeded.

In its report 233 I. C. C. 515, *supra*, at pages 522 and 533, the Commission stated that the report of its Bureau of Valuation showed the cost of reproduction of the system [fol. 696] properties, less depreciation, plus lands and rights, working capital, and net additions and betterments to December 31, 1936, as $147,717,268. If to this sum be added the net changes in investment accounts, reported in the carriers' annual reports for 1937 to 1940, inclusive, the

total becomes approximately $155,900,000. A substantial addition to this sum may be expected during 1941, especially from acquisitions of equipment. On the basis of original cost, as also stated in 233 I. C. C. 515, *supra*, the total as of December 31, 1936, was $178,024,641. Adding the net changes in investment for 1937-40, this would become $186,207,418.

It is recommended that the new capitalization shown on appendix A and summarized above be approved by the Commission.

The allocation of first-mortgage bonds in the recommended plan, shown in appendix A, is substantially on the basis of the proportions adopted in the court plan, except with respect to the claim of the Finance Corporation, which, as previously indicated, should be treated on the same basis as the R. G. Western first-trust bonds. Due to the reduction in the total amount of first-mortgage bonds below that shown in the court plan, the percentage of the claims of the Denver's senior bonds to be covered by new first-mortgage bonds is necessarily reduced. Since the effective date of the recommended plan is one year later than that of the court plan, the amount of the obligations to be provided for, including equipment trusts, is increased materially. Considering the first-mortgage bonds, income bonds, and stocks, the proportionate allocations conform substantially to the court plan, except with respect to the R. G. Western consolidated-mortgage bonds and the 4,111* shares of Salt [fol. 697] Lake stock outstanding in the hands of the public. The R. G. Western consolidated-mortgage bonds are entitled to the spill-over of any bonds issuable against the earnings of the R. G. Western first trusts in excess of the claims of the latter. An application of the debtor's earnings' formula to the amounts of new first-mortgage and new income bonds now contemplated, with an allowance for the stock of the Utah Fuel Company, indicates that the R. G. Western consolidateds are entitled to receive new income bonds for approximately 25 percent of the claim. The recommended plan provides accordingly, assigning new preferred stock to the remaining 75 percent of claim.

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* These shares comprise the 460 shares referred to in the Commission plan and the 3,651 shares released by the Finance Corporation.

Counsel for the trustee of the debtor's general-mortgage contend that the holders of the general-mortgage bonds should receive new common stock to the extent of 50 percent of their claim, based on facts brought out in the opinion of the court and at the further hearing before the Commission, largely relating to the improved condition of the railroad and its recent earnings record. It is true that the evidence introduced since the Commission announced its modified plan affords a basis for higher fixed charges and a larger total capitalization, as reflected in the plan herein recommended, but the claim represented by the general-mortgage bonds, including interest accruals to January 1, 1942, is so large that an increase of the percentage allocation of new common stock from 33⅓ percent to 50 percent would increase total capitalization to a prohibitive figure. As indicated in the Commission reports, no earnings were available for the general-mortgage bonds on the basis of the test-period year and the segregation formula.

The claim of the Chase National Bank on its loan of $1,500,000 has been computed on the basis of interest at 6 [fol. 698] percent from the date of the filing of the debtor's petition under section 77, in accordance with the contentions of the bank. This matter has not been determined by the courts. Subject to such determination, as stated in the Commission's modified plan, the note should be extended for a term of 10 years, bearing interest at 4 percent per annum, payable semiannually, but such interest should be contingent upon, and the payment thereof should be limited to, the total of interest and dividends paid by the new company on the collateral securing the new note or notes. The provisions of the Commission's modified plan for the claim of the Chase National Bank should be modified only with respect to the new collateral to be pledged, as shown in detail hereinafter.

The Railroad Credit Corporation in its recent brief explains that, as of June 30, 1941, the unpaid balance of the original loan of $500,000 had been reduced to $266,715.09, due to the application of distributive shares credited against the debtor's account arising out of the fund administered by the Credit Corporation, and the amount of unpaid interest was $904.88, making a total claim of $267,619.97. Explanation is also made of an error by the court in stating the amount of the Credit Corporation's claim as of January 1, 1941. For present purposes the claim of the Credit Cor-

poration, as of January 1, 1942, is computed at $268,953. The Credit Corporation objects to the court's proposal that its claim be paid in cash for the reason that it eliminates the option accorded the reorganization committee, under the Commission's plan, to extend the note in its discretion for not exceeding six months if payment in cash should not be made on the date of consummation of the plan, and also eliminates the provision for deducting the balance due the debtor under the marshaling and distributing plan. The [fol. 699] provision for the Credit Corporation claim as stated in the Commission's modified plan should be retained, with appropriate revision of the amounts of new securities issuable against the $662,000 of D. & R. G. consolidated-mortgage 4-percent bonds now under pledge, as shown in the summary later.

Sale of Stock for Future Control

The court plan provides for the issue of 379,049 shares of class-A common stock, having no par value, the beneficial interest in same to be distributed among the Denver's bondholders as indicated; the shares to be issued after five years and upon the expiration of a voting trust. The Finance Corporation would have the right during two years to convert the $6,000,000 of income bonds, taken by it at par in the new financing, into 100,000 shares of new class-B common stock. Such stock would be issued to the Finance Corporation only in the event a sale of control to connecting roads is arranged, subject to the condition that no more than 40 percent of the class-B stock should be sold to any one road. By this sale of stock the Finance Corporation would reimburse itself for the $6,000,000 of income bonds taken. If the conversion rights with respect to the class-B stock should be forfeited, the voting trust for the class-A stock might be continued by the court in order to insure satisfactory management for a stabilizing period, during which period the voting trustees would have the right of sale upon approval by the holders of two-thirds of the beneficial interests, but again subject to the condition that not more than 40 percent of the stock could be sold to any one purchaser.

The insurance group offers no objection to this part of the court plan except to suggest a condition to protect the [fol. 700] fair development, on equal terms, of the Denver

gateway and the Pueblo gateway. The Finance Corporation, on brief, points to the fact that before any railroad could acquire the class-B stock, authority must be obtained from the Commission under section 5, part 1, of the Interstate Commerce Act, within the 2-year period named, and if a contest should be started by another road the opportunity to sell the stock might be lost.

There is nothing of record to afford assurance that any Eastern carrier would purchase the stock, except the request of the trustee of the Missouri Pacific that only the new common stock of the reorganized Denver shall have voting rights and that the Missouri Pacific shall be afforded the right to acquire, upon fair and reasonable terms, one-half of such common stock. This request was concurred in by the chambers of commerce of Pueblo, Colorado Springs, and Salida, Colo., and by the city of Colorado Springs. The Missouri Pacific has indicated that it would not be interested in having a share in the control of the reorganized Denver unless it could purchase 50 percent of the stock.

The position of the Missouri Pacific trustee was known to the Commission when it announced its plan and consideration was also given to the arguments advanced in behalf of the debtor, the insurance group, and the various civic bodies to the effect that the plan should provide means whereby the proprietary companies might retain control of the Denver. As to voting rights of the new stock, however, the Commission should not approve the issue of any new preferred or common stock without voting power.

Other arguments were heard urging that the Burlington or the Rock Island should be given an opportunity to ac- [fol. 701] quire an interest in the reorganized Denver. In 233 I. C. C. 515, *supra*, at page 581, the Commission concluded that it was not its duty, in view of the finding that the present stockholders have no equity, to decide for the new owners what affiliations with other systems would be most advantageous, or to fix a price for stock to be sold. It was provided in the Commission's order of April 2, 1940, section K, that all the preferred stock and common stock of the new company, except directors' shares, should be deposited under an escrow agreement for a term of 10 years, and could be sold, subject to approval by the Commission and by not less than a majority of the holders of each class of stock, respectively.

Under the plan herein recommended the new financing may be provided either by the Finance Corporation or through private channels by means of a note, secured by adequate collateral. An analysis has been made, as described above, of the collateral securing the Finance Corporation's notes, the new securities assignable to this collateral have been indicated, and the element of strategic value in the cut-off has been recognized by allocating to the Finance Corporation, in the recommended plan, certain amounts of new first-mortgage bonds and income bonds rather than the securities allocable to the pledged bonds and stocks. From these considerations it does not appear that any valid basis exists for giving the Finance Corporation control of the new company, and, accordingly, the issue of a special class of stock carrying sole voting power is unnecessary. The Commission should adhere to its former conclusion regarding future control and should retain the provision for the voting trust for the preferred and common stocks as stated in section K of the order of April 2, 1940, *supra*.

[fol. 702] The court plan suggests that the common stock under that plan should not be sold except by consent of two-thirds of the holders of the beneficial interests, rather than a majority. This question was considered heretofore, and it is recommended that no change be made.

Reorganization committee

The order of April 2, 1940, *supra*, provided for a reorganization committee consisting of five members, two to be designated by the insurance group committee; one by the trustee under the debtor's refunding and improvement mortgage, one by the trustee under the general mortgage, and one by the Finance Corporation. The judge, pointing out that the properties of the debtor and secondary debtor are located almost wholly in the States of Colorado and Utah, urges that all the members of the reorganization committee be residents of these States, that all meetings of the committee be held in Denver, at the main office of the debtor, and that counsel for the committee, if any are necessary, shall be appointed by the court. Later, the judge expressed the opinion that the property should be under the direct control of the court until the reorganization is completed; also that the insurance group committee should be

represented by only one member on the committee and that the court or some other proper authority should name one member to represent the public interests of the citizens of Colorado. In its report in *St. Louis-S. F. Ry. Co. Reorganization*, 242 I. C. C. 323, the Commission ruled adversely upon a similar request for local representatives on a committee and concluded that those financially interested in the property should be permitted to make the appointments to the committee. It is recommended that no change be made in the provisions for the reorganization committee in the instant case.

[fol. 703] *Miscellaneous provisions*

In addition to placing the capital fund ahead of all fixed-interest payments, the judge urges that the annual depreciation charge on equipment should be set aside in a special cash fund and used only to take care of interest and principal payments on equipment-trust obligations now outstanding or hereafter issued, and to take care of, in whole or in part, the purchase, building, or improvement of equipment. These provisions are stated to be the best guarantees that can be put into the plan to assure the proper upkeep and maintenance of the property.

It is recommended that no change should be made in the Commission's plan regarding payments into the capital fund. With the virtual completion of the improvement program, including new equipment, the suggestion of the judge as to placing the payments into the capital fund ahead of fixed interest and the impounding of equipment depreciation charges do not appear to be necessary. However, if, after the new plan shall have been certified to the court, the judge is still of the view that these changes should be made in the plan, it should be provided that he may introduce them without returning the plan to the Commission.

Another unusual feature of the court plan is in connection with the interest on the new 4½-percent income bonds. The court proposes that this interest shall accumulate only to the extent of three-fourths of the income available for the payment thereof. It would seem, as pointed out in the brief of the insurance group, that the purpose of this provision may have been to permit the company to apply more of its income to additions and betterments than would be the case under the interest provisions of the Commission

[fol. 704] plan for the new income bonds. The proposal appears unnecessary and should not be adopted.

In connection with the new first-mortgage bonds to be issued in the reorganization, the Commission's plan, 239 I. C. C. on page 501, provided that additional bonds shall be issuable under certain conditions, and included the following:

> (2) When on any interest payment date the aggregate principal amount of first-mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either 35 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the mortgage trustee as a sinking fund a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, the payment to the capital fund, contingent interest, and sinking-fund payments for the retirement of income bonds as hereinafter prescribed.

Counsel for the insurance group suggest that the foregoing percentage figures of 35 percent and 60 percent be increased to 45 percent and 70 percent, respectively, so that "this sinking fund will constitute only a practical check on injudicious financing rather than a harsh and impracticable constraint on the new company." In none of his opinions did the judge refer to these percentages, nor has any of the parties, except the committee, objected to them. The figures were adopted in the approved plan after care-[fol. 705] ful consideration by the Commission and should not be modified.

Counsel for the committee further suggest that the following provision of the Commission's plan (page 600) for the new first-mortgage bonds should be omitted;

> (4) No additional bonds of series A other than those to be issued under the plan may be issued, and no bonds may be issued of any series having a maturity on or before the maturity of the bonds of series A, except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition.

Counsel further suggest the omission of the corresponding provision (page 602) for the new income bonds reading:

> (3) no income bonds other than those issued in connection with the plan shall be issued having a maturity on or before the maturity of the initial issue, except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition.

These suggested omissions may be for the purpose of removing an apparent conflict with the following provision in the Commission's plan (pages 599 and 601) for the first-mortgage bonds, and a similar provision for the income bonds:

> Additional bonds shall be issuable under the mortgage without limit as to amount, or within such limit as may be specified in the mortgage, having such dates, maturities, coupon rates, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission.

[fol. 706] The conflict arises from the inclusion of "maturities" without qualification, and should be removed by revising the language in connection with the first mortgage provision to read: "maturities (subject to the restriction stated under (4) below)". A similar revision should be made in the case of the income bonds, as hereinafter provided.

It is recommended that a general sinking fund be provided for the new first-mortgage bonds, the annual payments to equal one-half of 1 percent of the maximum principal amount of such bonds at any time authenticated and delivered, including bonds under pledge.

Debtor's Position

Despite the Commission's finding that the debtor's stockholders have no equity, and the court's failure to find otherwise, the debtor still contends that an equity of at least $40,000,000 exists, that no reorganization can be accomplished without a valuation of the property, and that the fairness of the court plan cannot be determined without such valuation. However, various specific objections to the court plan are offered, such as its recognition of interest accruals in excess of $7,000,000 since September 1, 1935, the

treatment of the Finance Corporation, the provision for sale of control, and the inclusion of the Junction, which is not a debtor under section 77. The debtor states that it "reserves its objections to the proceedings going forward before the Commission or the court until a new plan or plans are filed, the feasibility thereof determined, and hearings thereon ordered in accordance with subsection (d) of section 77 of the Bankruptcy Act."

The debtor's general position with respect to the purpose and scope of section 77, and the rights of creditors and [fol. 707] stockholders, was stated in 233 I. C. C. 515, *supra*, at pages 573 and 578, and requires no further comment. The main features of the court plan have been considered herein and conclusions recommended, except as to the propriety of including the Junction in the plan. All the plans which have been promulgated, including the court plan, have assumed that the Junction could be merged with the debtor in this reorganization, although the Junction is not in trusteeship under section 77. It has no separate operating organization. It is operated under lease by the debtor, and the leasehold interest is in trusteeship. Its stock is pledged under the debtor's refunding and improvement mortgage. The Central Hanover Bank & Trust Company is trustee of the Junction first mortgage, as well as the R. G. Western first-trust mortgage. Throughout the entire proceedings before the court and the Commission, counsel for Central Hanover Bank have discussed the claims of both classes of bondholders on the same basis with respect to the plan and the rights of these bondholders, without reference to the fact that the Junction is not in trusteeship. The court disregarded it also in preparing its plan. The Commission should not attempt to adjudicate the matter but should provide in the plan for the inclusion of the Junction if legally possible.

Summary

The Commission should approve a new plan in accordance with the foregoing recommendations and an appropriate order should be entered adopting the revisions in the order of April 2, 1940, indicated below.

A. The effective date of the plan should be January 1, 1942.

[fol. 708] B. This section should be modified to read:

> Consolidation of The Denver and Salt Lake Railway Company, hereinafter called the Salt Lake, with the

debtor's properties shall be undertaken and shall be effective if, and only if, the holders of at least 66⅔ percent in aggregate principal amount of Salt Lake income bonds voluntarily consent, within 90 days of the submission of the proposal to them, to (1) an extension of the maturity to that of the first-mortgage series-A bonds to be issued by the new company, (2) the modification of interest terms to fixed interest of 4 percent per annum; and prior contingent cumulative interest of 2 percent per annum, payable when fixed and contingent interest, respectively, on the new first-mortgage bonds become payable, and (3) the call for payment or for refunding (at the convenience of the reorganized company) of income bonds not consenting. In the event of such consolidation with the Salt Lake the tunnel contract shall be assumed by the reorganized company and the present trackage agreement canceled; the properties to be consolidated will then be those of the debtor, the secondary debtor, the Rio Grande Junction Railway Company, hereinafter called the Junction, the Goshen Valley Railroad Company, and the Salt Lake. These properties shall be merged or consolidated to the extent legally possible by transfer of the subsidiary properties to the reorganized debtor or by transfer of all the properties to a new corporation organized for the purpose, hereinafter referred to as the new company. Unless such consents are obtained from the holders of the Salt Lake income bonds within the period stated, no actual consolidation of the Salt Lake and the Salt [fol. 709] Lake Western with the debtor will be effective, and in that event only the properties of the debtor, the Junction, and the Goshen Valley shall be merged or consolidated in the manner indicated above; no provision will be made for the Salt Lake stock held by the public, and the trackage agreement will remain in effect.

C. The capitalization of the new company, as of January 1, 1942, should be restated to conform to that recommended herein.

D. This section, referring to the surrender of existing securities, should be modified to read as follows:

Upon the consummation of the plan, including consolidation with the Salt Lake, and the issue, distribution,

and modification of securities as herein provided, the existing stocks of the debtor and its affiliated companies, together with all mortgage bonds issued and outstanding, including bonds pledged, and excluding all bonds of the Salt Lake, shall be surrendered to the reorganization committee and canceled, and all mortgages, other than the Salt Lake, shall be satisfied of record and canceled. In the event that consolidation of the Salt Lake is not effected, the stocks to be surrendered and canceled shall not include those of the secondary debtor and the Salt Lake.

E. The first paragraph of this section of the order, regarding the lien of the new first-mortgage bonds, should be modified to read as follows:

(E). The new first mortgage shall constitute a first lien, subject only to the lien of equipment-trust obligations, on (1) all property owned by the debtor, the secondary debtor, (in the event that consolidation with the Salt Lake is effected, otherwise excluding the sec- [fol. 710] ondary debtor) or their trustees in bankruptcy as such, the Junction, and the Goshen Valley, at the time of effectuation of the plan, including securities, equipment, and the equity in such equipment as may be subject to equipment-trust obligations, but excluding the narrow-gage railway lines of the debtor, and equipment and property essential to the operation thereof, and excluding also the capital stock of the Utah Fuel Company; and (2) all property acquired by the new company after the date of the new first mortgage for use on or in connection with the mortgaged property subject only to such encumbrances or purchase-money liens as may exist or be created at the time of acquisition. So far as the reorganization committee hereinafter provided for may deem practicable, such lien shall be in the form of a direct mortgage, but it may take the form of the pledge or assignment of securities of a corporation or corporations owning property to which the lien is intended to extend. In the event of the consolidation of the properties of the Salt Lake as a part of the new system, the new first mortgage shall constitute a lien on such properties subject to the lien of the Salt Lake first-mortgage bonds and income bonds.

The provision in the third paragraph for the issue of first-mortgage bonds should be modified to read as follows:

> The first-mortgage bonds may be issued in series, all equally secured as to principal and interest. Approximately $34,579,366 of series-A bonds shall be issued in connection with the reorganization in partial settlement of claims, and additional bonds as may be necessary for [fol. 711] the purpose of pledge or for sale in connection with new financing, as provided in the plan. The series-A bonds shall have a term of 50 years and shall bear fixed interest at the rate of 3 percent and contingent interest in addition at the rate of 1 percent per annum, fully cumulative, both payable semiannually.

The first part of the fourth paragraph under section E should be modified to read as follows:

> Additional bonds shall be issuable under the mortgage without limit, or within such limit as may be specified in the mortgage, having such dates, maturities (subject to the restriction stated in (4) below), coupon rates, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by the Commission. Such additional bonds shall be issuable on such bases, including the refunding of debt and the deposit of cash as shall be prescribed in the mortgage . . .

The following new provision should be introduced under section E of the order:

> A sinking fund shall be provided for retirement of first-mortgage series-A bonds to be issued in the reorganization, the annual payments to be equal to one-half of 1 percent of the largest principal amount of such bonds at any time authenticated and delivered, including bonds under pledge, such payments to be made if the available net income for the previous year is sufficient therefor after payment of all fixed charges and payment into the captial fund, but before payment of contingent interest. Such payments shall not be cumulative. The sinking fund shall be applied to the retire- [fol. 712] ment of first-mortgage series-A bonds by purchase at not exceeding the current redemption price plus

accrued interest, or by redemption. All first-mortgage bonds of series-A so acquired shall be canceled and no bonds of any kind issued to refund them.

In accordance with this provision, paragraph (d) under section G of the order should be modified to read as follows:

(d) All payments to sinking funds established or which may have been established, as provided above, for the retirement of first-mortgage bonds.

F. The opening provisions in the second paragraph of this section, applying to the new income bonds, should be modified to read as follows:

The income-mortgage bonds may be issued in series, all equally secured as to principal and interest. Approximately $34,925,295 of series-A income bonds shall be issued in the reorganization in partial settlement of claims, and additional bonds as may be necessary for the purpose of pledge, as provided in the plan. Additional bonds of other series shall be issuable without limit as to amount, or within such limit as may be specified in the mortgage, having such dates, maturities (subject to the restriction stated under (3) below), rates of contingent interest, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission * * *.

G. The date December 31, 1938, in the second paragraph of this section should be changed to June 30, 1941.

[fol. 713] The opening clause of the third paragraph of this section should be modified to read as follows:

(a) All fixed charges, determined in accordance with such accounting rules or practice of the new company accrued during such income period, including fixed-interest payments on the Salt Lake first-mortgage bonds and income bonds in the event consolidation with the Salt Lake is effected under the plan; provided howev- * * *

The following new matter should be added to the end of paragraph (e) of this section:

and provided further, that the court may alter the foregoing, without returning the plan to the Commis-

sion for revision, to the extent of placing the payments into the capital fund ahead of all payments of fixed interest, and, on the same basis, the court may make appropriate provision in the plan for the establishment and maintenance of a special fund representing the charges to depreciation of equipment, for use in acquiring new equipment or making additions and betterments to existing equipment.

Under (d) of this section of the order, after the sentence, "the available net income for each income period shall be applied to the following purposes and in the following order", there should be inserted a new provision for the application of available net income, and minor changes should be made in others, so that the former subsections (1), (2), (3), and (4) shall be modified to appear as follows:

(1) All available net income shall, to the extent required, and subject to the provision hereinbefore made for payment in even multiples of one-fourth of 1 percent and postponement of fractional surplus, be applied to the payment, on April 1 in each year, of prior [fol. 714] contingent interest at the rate of 1 percent per annum prorata on the first-mortgage bonds, series A, of the new company then outstanding and on the modified Salt Lake income bonds outstanding, in the event of consolidation with the Salt Lake; otherwise on the first-mortgage bonds of the new company only.

(2) All available net income shall, to the extent required and subject to the provision hereinbefore made for payment in even multiples of one-fourth of 1 percent and postponement of fractional surplus, be applied in the payment on April 1 of each year to interest on the then outstanding income-mortgage bonds of the new company, excluding bonds then held in the sinking fund under the new income mortgage, but including bonds under pledge, accruing during the income period ending on the next preceding December 31, and to the payment of any unpaid accumulated interest on said bonds.

Former subsection (2) should be revised only in its opening lines, which should read as follows:

(3) Any then remaining available net income shall be applied, until all the income bonds of the new company

shall have been retired, on April 1 in each year, to a sinking fund * * *.

Former subsections (3) and (4) should be changed to (4) and (5), respectively, and the text should remain unchanged.

In the paragraph following (5), the first date June 30, 1938, should be changed to December 31, 1941, and the second date June 30, 1938, should be changed to January 1, 1942.

[fol. 715] The concluding paragraph under section G should be modified to read as follows:

> (c) For the purpose of paying fixed interest on the bonds outstanding under the new first mortgage in a year or years in which the net earnings of the new company available for interest on said bonds shall be inadequate for the payment of such interest, and only to the extent of such inadequacy.

Section H of the order, describing stocks of the new company, should be modified in respect of the preferred stock (1) to provide that approximately 290,136 shares shall be issued in the reorganization, excluding shares which may be issued for pledging purposes, and (2) to change the beginning of the calendar year in respect of which dividends may first be paid at the rate of 5 percent from January 1, 1939, to January 1, 1942.

The provisions for the new common stock should be modified to read as follows:

> The common stock of the new company shall be authorized in the amount of 1,000,000 shares, of no par value, of which approximately 428,406 shares shall be issuable in the reorganization, excluding shares to be pledged, and approximately 290,136 shares shall be reserved for conversion of the preferred stock.

Section I of the order should be revised to show the amounts and kinds of new securities to be issued for settlement of the claims of each class of bond-holders and the stock of the Salt Lake held by the public in the event consolidation takes place, all according to the plan herein recommended. The first two paragraphs of section I would then read as follows:

> [fol. 716] I. The holders of bonds of the classes shown below shall receive for each $1,000 bond and all unpaid

interest thereon, as of the effective date of the plan, the following amounts of new securities:

Rio Grande Western Railway Company first-trust bonds, $728.77 of new first-mortgage bonds and $551.23 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $322.50 of new income bonds and $967.50, par value, of new preferred stock; Junction first-mortgage bonds, $757.63 of new first-mortgage bonds and $571.54 of new income bonds; Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $260 of new first-mortgage bonds, $260 of new income bonds, $260, par value, of new preferred stock, and 5.2 shares of new class-A common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $267.50 of new first-mortgage bonds, $267.50 of new income bonds, $267.50, par value, of new preferred stock, and 5.35 shares of new class-A common stock; the debtor's refunding and improvement 5-percent bonds, $272.50 of new first-mortgage bonds, $272.50 of new income bonds, $272.50, par value, of new preferred stock, and 5.45 shares of new common stock; the debtor's refunding and improvement 6-percent bonds, $287 of new first-mortgage bonds, $287 of new income bonds, $287, par value of new preferred stock, and 5.74 shares of new common stock; the debtor's general-mortgage bonds, 4.69 shares of new common stock.

Section I should be further modified as follows:

By elimination of the provision for redemption of the [fol. 717] Salt Lake first-mortgage bonds and income bonds;

By revising the provision for the claim of the Railroad Credit Corporation only in respect of the securities to be issued in exchange for those now under pledge, the modification to show $172,120. of new first-mortgage bonds, $172,120 of income bonds, $172,120, par value, of new preferred stock, and 34.424 shares of new common stock;

By revising the provision for the claim of the Chase National Bank to provide that the new note or notes shall be in face amount equal to that of the present note plus interest accrued to December 31, 1941, in the amount allowed by the court, and by changing the amounts of new securities issuable as collateral so that they will be in

accordance with the recommended plan, viz, $1,661,160 of new first-mortgage bonds, $1,661,160 of new income bonds, $1,661,160, par value, of preferred stock, and 33,223 shares of common stock;

By modifying the provision for payment of the notes to the Finance Corporation, stating the total amount of the claim with interest to January 1, 1942, and the amounts and kinds of new securities issuable, in full settlement of this claim, against the collateral now held by the Finance Corporation, as hereinbefore shown, viz., on the basis of consolidation with the Salt Lake, $7,570,431 of new first-mortgage bonds and $5,711,027 of income bonds. On the basis of continuing separate operation of the Salt Lake under the trackage agreement, the new securities issuable to the Finance Corporation in respect of the debtor's bonds held as collateral should be $1,039,300 of new first-mortgage bonds, $1,386,650 of income bonds, $2,079,850, par value, of preferred stock, and 20,672 shares of common stock, and in respect of the remainder of the Finance Corporation [fol. 718] claim a 12-year collateral note shall be issued by the new company in the principal amount of $7,500,000, secured by pledge of the $1,266,000 of Salt Lake income bonds, $1,777,000 of Rio Grande Southern first-mortgage bonds, 73,710 shares of Denver-Colorado Springs-Pueblo Motor Way stock, 1,564 shares of Rio Grande Motor Way stock, 36,310 shares of Salt Lake Western stock, and 45,889 shares of Salt Lake stock now pledged with the Finance Corporation. The provisions regarding the payment of interest on this note and the obligation of the new company with respect to interest and principal should be as hereinbefore stated.

The paragraph in the order following the provision for settlement of the claim of the Finance Corporation should be modified to read as follows:

> The $5,000,000 of trustees' certificates outstanding shall be paid in cash in the manner described below. The expenses of reorganization not heretofore paid shall be paid out of the debtor's funds.

Section J of the order, referring to cash financing in connection with the reorganization should be modified to read as follows:

> J. The requirements for new cash in connection with the reorganization shall be for the purpose of paying

the $5,000,000 of trustees' certificates outstanding, and, in the event the holders of the required percent of Salt Lake income bonds shall accept the proposal for modification of interest, for the payment, purchase, or refunding of income bonds the holders of which do not assent to such proposal. The necessary and reasonable amount of cash required for these purposes shall be determined by the reorganization committee, sub-
[fol. 719] ject to approval by the court. The funds shall be advanced by the Finance Corporation or obtained through private channels and evidenced by a collateral note of the new company for a term of 12 years secured by pledge of new first-mortgage bonds in an amount equal to 125 percent of the amount of the loan; or such other amount of bonds as may be required by the lender and approved by this Commission. As an alternative to such a loan, not exceeding $10,000,000 of new first-mortgage bonds may be issued for sale to provide the new money required, under terms and conditions determined by the reorganization committee and approved by the court and this Commission.

The second paragraph of section L of the order, regarding the assumption by the new company of obligations with respect to agreements and contracts which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding, etc., should be prefaced by the following opening phrase:

> In the event consolidation of the various companies, including the Salt Lake, shall be effected, as herein provided, * * *

The paragraph, as thus modified, should be supplemented by the following new statement:

> In the event consolidation of the Salt Lake is not effected, the foregoing provisions for assumption of the lease agreements with the Northwestern Terminal Railroad Company and with the Moffat Tunnel Improvement District shall not apply, and the assumption of obligation by the new company with respect to agree-
> [fol. 720] ments and contracts shall be confined to those of the debtor and its affiliated companies other than the Salt Lake.

Section N of the order should be modified by changing the stated effective date of the plan from June 30, 1938, to January 1, 1942, and revising the closing sentence to read as follows:

> The merger or consolidation of the properties, including the Salt Lake if the proposal is accepted by the holders of the required percent of bonds, should be effected in a manner to be determined by the reorganization committee, subject to approval by the Commission and the court, and under a fair and equitable arrangement to protect the interests of the railroad employees affected, as required by law.

The following ordering cause should be eliminated:

It is further ordered, That, except insofar as the modifications of plan herein approved are modifications sought in the aforesaid petitions, such petitions be, and they are hereby, denied.

And it should be stated in the new order that such order supersedes the orders of July 11, 1939, and April 2, 1940.

Filed Sept 2, 1941. G. Walter Bowman, Clerk.

(Here follows 2 pasters, side folios 721-722, 723)

[fols. 721-722]

APPENDIX A.

Recommended plan, on basis of consolidation with the Denver & Salt Lake
Pledged securities omitted

D. & R. G. W.	Claims as of Jan. 1, 1942	Undisturbed or extended	First mortgage bonds; 3% fixed interest, 1% prior contingent interest	Income bonds 4½% interest	Preferred stock 5%	Common stock no-par-value; shown here at $100 a share
Equipment obligations	$8,254,825	$8,254,825				
R. G. West. first 4's, with interest	19,443,200		57% 11,070,000	43% 8,373,200		
R. G. West. consol. 4's, with interest	19,453,200			25% 4,863,300	75% 14,589,000	
R. G. June. first 5's, with interest	2,658,333		57% 1,515,250	43% 1,143,083		
D. & R. G. consol. 4's, with interest	44,362,500		20% 8,872,500	20% 8,872,500	20% 8,872,500	40% 17,745,000
D. & R. G. consol. 4½'s, with interest	8,535,925		20% 1,707,185	20% 1,707,185	20% 1,707,185	40% 3,414,370
Refunding and impt. 5's, with interest	16,350,000		20% 3,270,000	20% 3,270,000	20% 3,270,000	40% 6,540,000
Refunding and impt. 6's, with interest	2,870,000		20% 574,000	20% 574,000	20% 574,000	40% 1,148,000
General 5's, with interest	41,979,600					33⅓% 13,993,200
Chase Nat. Bank note, with interest	*2,068,458	[2] 2,068,458				
R. R. Credit Corp. note, with interest	*268,953	[2] 268,953				
R. F. C. notes, with interest	*13,281,458		57% 7,570,431	43% 5,711,027		
Unsecured claims	*440,000					
Trustees' certificates	5,000,000	[3] 6,000,000				
Reorganization expenses	*500,000	pay in cash				
Totals, D. & R. G. W.		16,592,236	34,579,366	34,514,295	29,013,585	42,840,570
Denver & Salt Lake—Stock		4,111 sh.		411,000		
First-mtge. 4% bonds	1,500,000	[4] 1,500,000		34,925,295		
Income bonds 6%	9,734,000	[5] 9,734,000				

Summary of Recommended Plan

New capital structure

Equipment obligations	$8,254,825
Chase Bank note, extended	2,068,458
Railroad Credit Corporation note, approximate	268,953
Loan for new money, approximate	6,000,000
New first-mortgage bonds	34,579,366
D. & S. L. first mortgage bonds	1,500,000
D. & S. L. income bonds	9,734,000
	62,405,602
New 4½ percent income bonds	34,925,295
Total debt	97,330,897
Preferred stock	29,013,585
Common stock at $100	42,840,570
	169,185,052

Annual charges

	Fixed	Prior Contingent	Contingent	Preferred Dividends
Equipment obligations	$195,000			
Chase Bank note	49,835	$46,612	$46,150	
R. C. C. note	2,690			
Loan for new money, approx.	240,000			
New first-mtge. bonds	1,037,381	345,794		
D. & S. L. first-mtge. bonds	60,000			
D. & S. L. income bonds	389,360	194,680		
New income bonds			1,571,638	
New preferred stock				1,450,679
	1,974,266	587,086	1,587,788	1,450,679
Capital fund		750,000		
Sinking fund first mtge.		172,897		
Sinking fund income mtge.			87,313	

* Subject to adjustment.

[1] Chase Bank note, as extended, will be secured by pledge of
- New first-mortgage bonds $1,661,160
- New income bonds 1,661,160
- New preferred stock 1,661,160
- New common stock ..... 33,223 shs.

[2] Railroad Credit Corporation note, if extended, will be secured by pledge of
- New first-mortgage bonds $172,120
- New income bonds 172,120
- New preferred stock 172,120
- New common stock ..... 3,443 shs.

[3] Tentative amount of loan from the Finance Corporation or others to provide funds for paying $5,000,000 of trustees' certificates and for other purposes as described in the plan.

[4] The Salt Lake first-mortgage bonds will remain undisturbed whether or not consolidation with the Salt Lake is effected, but in the event of consolidation the interest obligation will be on a parity with the fixed interest on the first-mortgage bonds of the new company.

[5] The Salt Lake income bonds will remain undisturbed as to lien. Consolidation will be effected if the holders of at least 66⅔ percent of the bonds consent, within 90 days of the submission of the proposal, to an extension of the maturity to the maturity date of the first-mortgage bonds of the new company and to a modification of the interest terms to 4 percent fixed interest and 2 percent prior contingent interest, both on a parity with fixed and prior contingent interest on the first-mortgage bonds of the new company. In the event of rejection of the proposal, the Salt Lake income bonds will remain undisturbed in every respect.

[Ed. 723]

Appendix 4

Suggested Plan
In Modification of Proposed Report

	Total Claim 1-1-42	Undisturbed or Extended	First Mtg. Bonds 3%-1%	% of Total Claim	Income Bonds	% of Total Claim	Preferred Stock	% of Total Claim	Common Stock	% of Total Claim
Equipment Obligations	$8,254,825(8)	$8,254,825(8)								
R. G. W. 1st 4's	19,443,200		$14,728,854	75.75	$4,714,346	24.25				
R. G. W. Consol 4's	19,453,200				5,835,960	30.00	$13,617,240	70.00		
R. G. J. 1st 5's	2,658,333		1,963,300	73.85	695,033	26.15				
D. & R. G. Consol 4's and 4½'s	52,898,425		14,026,121	26.51	10,579,685	20.00	11,212,671	21.20	$17,079,948	32.29
R. & I. 5's and 6's	19,220,000		4,971,599	25.87	3,844,000	20.00	4,073,988	21.20	6,330,413	32.93
General 5's	42,352,200								20,085,102	47.42
R. F. C.	13,281,458		4,255,671(1)	32.04	9,025,787	67.96				
Chase Bank Note	2,068,458	2,068,458(9)								
R. C. C. Note	268,953	268,953(10)								
Unsecured Claims	440,000									
Trustees Certificates	5,000,000	4,000,000(2)								
Reorganization Expenses	500,000(3)									
D. & S. L. Minority Stock	4,111 sh.				411,100					
D. & S. L. 1st 4's	1,500,000	1,500,000(4)								
D. & S. L. Incomes	9,734,000	9,734,000(5)								
Total			$39,945,545(6)		$35,105,911(6)		$28,903,899(6)		$43,495,463(6)	
Charges:(11)										
Equipment Trust's		$195,000(8)								
Interest on New Money Bonds		160,000								
Interest on D. & S. L. 1st 4's		60,000								
Fixed Interest on D. & S. L. Income's		292,020								
Fixed Interest on New First's			1,269,720							
Total Fixed Interest			$1,976,740							
Capital Fund			750,000							
Prior Cont. Int.—New First's			423,240							
Prior Cont. Int.—D. & S. L. Income's			97,340							
Total Prior Cont. Int.			$520,580							
First Mtg. Sinking Fund			236,620(7)							
Total Through 1st Mtg. S. F.			$3,483,940							
Income 4½'s Interest					1,662,264					
Income Mtg. Sinking Fund					92,348					
Total Charges before Pfd. Div.					$5,238,552					
Preferred Dividend							1,542,343			
Grand Total							$6,780,895			

(1) Indicated distribution for collateral other than Denver Bonds considered as constant (per Court Plan); the change reflects decrease of distribution to system collateral. The new first mortgage bonds issuable in respect of the pledged Denver bonds are $9,696 for the Trust's, $270,028 for the Eastern Consol's and $1,546,654 for the R. & I.'s.

(2) Assumes $2,000,000 Trustees Certificates will have been paid in cash.

(3) To be paid in cash from treasury.

(4) Undisturbed—4% interest.

(5) 3% fixed, 1% prior contingent interest. $1,266,000 additional principal amount (representing the Salt Lake Income's pledged with RFC) are to be pledged under the new First Mortgage.

(6) Like Proposed Report, excludes pledged securities.

(7) Includes ½ of 1% on $5,000,000 New 1st Mtg. bonds pledged for New Money Bonds and $42,323,993 New 1st Mtg. bonds outstanding and pledged for Chase and R. C. C. Notes.

(8) The actual amount will be only $6,472,000 for principal and $151,853 for interest, but the Examiner's figures are retained for ease of comparison.

(9) This will be secured by $2,150,149 first mortgage bonds, $1,661,160 income bonds, $1,760,547 of preferred stock and $2,733,944 of common stock (at $100 per share).

(10) Subject to reduction by distributions under Marshalling Plan. To be secured by $228,299 of first mortgage bonds, $172,120 of income bonds, $182,418 of preferred stock and $277,763 of common stock.

(11) Figures include charges on all securities pledged for Chase Bank and R. C. C. Notes.

(Clerk's Note: This Appendix 4 was part of the brief on exceptions of Insurance Group Committee Filed on October 8, 1941 before the Interstate Commerce Commission.)

[fol. 724] IN UNITED STATES DISTRICT COURT

STATEMENT OF ASSETS AND LIABILITIES OF DEBTOR AS OF CLOSE OF BUSINESS ON MAY 31, 1943, AND OF ITS REVENUES AND EXPENSES FOR THE MONTH OF MAY, 1943

Pursuant to Paragraph (6) of Order No. 1 entered herein on November 1, 1935, the undersigned Trustees of the Debtor, The Denver and Rio Grande Western Railroad Company, file herewith a statement of its assets and liabilities as of the close of business on May 31, 1943; and a statement of its revenue and expenses for the month of May, 1943; said statements being certified as correct by the [fol. 725] chief accounting officer of the Debtor.

Dated July 6, 1943.

Wilson McCarthy and Henry Swan, as Trustees of The Denver and Rio Grande Western Railroad Company, by Henry McAllister, Their Attorney.

[fol. 726]

The Denver and Rio Grande Western Railroad Company
(Wilson McCarthy and Henry Swan, Trustees)

General Balance Sheet Statement

As of May 31, 1943

Assets

	Book Assets Total	Company's Own Issues		
Investments:				
701 Road and Equipment Property			229,723,795 88	
702 Improvements on Leased Property			507,235 52	
702½B Donations and Grants			(Cr.) 1,963,049 00	
703½ Special Reserve Funds—Pennsylvania Company—Equipment			9,188 19	
704 Deposit in Lieu of Mortgage Property Sold			37,874 64	
705 Miscellaneous Physical Property			231,132 45	
706 Investments in Affiliated Companies—Pledged			14,416,907 16	
706 Investments in Affiliated Companies—Unpledged			2,049,377 56	
707 Other Investments			734 00	245,013,196 34

[fol. 727]

Current Assets:				
708 Cash			10,276,854 87	
709 Temporary Cash Investments			4,200,000 00	
711 Special Deposits			965,592 84	
714 Net Balance Receivable from Agents and Conductors			606,048 20	
715 Miscellaneous Accounts Receivable			5,003,727 74	
716 Material and Supplies			5,252,296 91	
718 Rents Receivable			112,800 00	
719 Other Current Assets			48,884 05	26,465,204 61
Deferred Assets:				
720 Working Fund Advances			5,375 80	
722 Other Deferred Assets			526,962 31	532,338 11
Unadjusted Debits:				
723 Rents and Insurance Premiums Paid in Advance			64,244 08	
727 Other Unadjusted Debits			5,982,761 13	6,047,005 21
728 Securities Issued or Assumed—Unpledged—Held by Company	12,400 00	12,400 00		
729 Securities Issued or Assumed—				
Pledged (Redeemed—Held by Trustee)	8,333,000 00	8,333,000 00		
Pledged (Held as Collateral)	13,331,000 00	13,331,000 00		
	21,664,000 00	21,664,000 00		
	21,676,400 00	21,676,000 00		
				278,057,744 27

[fol. 728]

Liabilities

	Book Liability	Portion Held by or for Company		
Stock:				
751 Capital Stock:				
Common	62,457,539 62		62,457,539 62	
Preferred	16,445,600 00	12,400 00	16,433,200 00	
752 Stock Liability for Conversion	12,400 00		12,400 00	
Total	78,915,539 62	12,400 00	78,903,139 62	
Long Term Debt:				
755 Funded Debt Unmatured	70,764,000 00	11,876,000 00	58,888,000 00	
755½ Debt in Default	62,783,000 00	1,455,000 00	61,328,000 00	
756½ Equipment Obligations	5,487,000 00		5,487,000 00	
757 Amounts Payable to Affiliated Companies	4,355,174 38		4,355,174 38	
Total	143,389,174 38	13,331,000 00	130,058,174 38	
Total Capital Liabilities	222,304,714 00	13,343,400 00	208,961,314 00	208,961,314 00

[fol. 729].

Current Liabilities:			
758 Loans and Bills Payable		3,485,000.00	
759 Traffic and Car-Service Balances—Cr.		1,723,701.71	
760 Audited Accounts and Wages Payable		3,356,645.12	
761 Miscellaneous Accounts Payable		934,159.96	
762 Interest Matured Unpaid		101,737.50	
764 Unmatured Interest Accrued		35,665.84	
766 Unmatured Rents Accrued		205,602.76	
767 Accrued Tax Liability		6,442,676.00	
768 Other Current Liabilities		124,833.89	16,410,022.78
Deferred Liabilities:			
769½ Interest in Default		48,480,542.40	
770 Other Deferred Liabilities		306,945.41	48,787,487.81
Unadjusted Credits:			
772 Premium on Funded Debt		11,320.02	
775½ Accrued Amortization of Defense Projects—Road		10,105.27	
776 Accrued Depreciation—Road and Equipment		16,054,699.69	
776½ Accrued Amortization of Defense Projects—Equipment		1,107,976.13	
778 Other Unadjusted Credits		758,704.70	17,942,805.81
Surplus:			
786 Earned Surplus		(Dr.) 14,043,886.13	
Total Surplus			(Dr.) 14,043,886.13
			278,057,744.27

Certified as correct this 6th day of July, 1943.

T. A. Thompson,
General Auditor.

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The Denver and Rio Grande Western Railroad Company
(Wilson McCarthy and Henry Swan, Trustees)

Revenues and Expenses

(May, 1943)

Income Statement

	Month of May, 1943	Five Months
Railway Operating Income:		
Railway Operating Revenue:		
Transportation—Rail Line:		
101 Freight	4,990,724.90	22,969,022.80
102 Passenger	731,793.83	3,817,959.76
103 Baggage	760.99	3,182.59
105 Parlor and Chair Car	102.15	563.09
106 Mail	34,092.21	166,975.86
107 Express	78,719.92	273,424.21
108 Other Passenger—Train	1,072.00	5,202.72
109 Milk	3,884.61	19,114.33
110 Switching	27,392.76	145,290.53
Incidental:		
131 Dining and Buffet	78,809.50	398,421.83
132 Hotel and Restaurant	4,913.20	21,483.89
133 Station and Train Privileges	2,640.31	11,034.90
134 Parcel Room	229.30	1,137.80
135 Storage—Freight	79.40	1,921.43
136 Storage—Baggage	175.00	738.74
137 Demurrage	7,414.70	33,390.20
138 Telegraph and Telephone	292.50	1,241.15
142 Rents of Buildings and Other Property	1,982.75	8,373.66
143 Miscellaneous	6,538.24	28,524.98
Joint Facility:		
151 Joint Facility—Cr.	6,849.73	33,115.57
152 Joint Facility—Dr.	3,104.37	17,020.04
Total Railway Operating Revenues	5,975,363.63	27,918,100.00

[fol. 731]

Railway Operating Expenses:				
Maintenance of Way and Structures		470,523.07		2,074,064.84
Maintenance of Equipment		910,170.73		4,447,875.44
Traffic		89,455.29		461,438.27
Transportation—Rail Line		1,591,767.09		7,772,834.24
Miscellaneous Operations		54,549.64		290,880.68
General		110,360.03		529,149.76
Total Railway Operating Expenses		3,226,825.85		15,597,243.23
Net Revenue from Railway Operation		2,748,537.78		12,320,856.77
532 Railway Tax Accruals		1,028,601.93		4,534,300.30
Railway Operating Income		1,719,935.85		7,786,556.47
Rent Income:				
504 Rent from Locomotives		7,241.57		39,860.30
505 Rent from Passenger—Train Cars		3,747.46		16,599.04
507 Rent from Work Equipment		3,065.53		9,391.12
508 Joint Facility Rent Income		49,680.20		245,713.60
Total Rent Income		63,734.76		311,564.06
Rents Payable:				
536 Hire of Freight Cars—Debit Balance		82,535.60		397,947.66
537 Rent for Locomotives		28,809.91		188,966.33
538 Rent for Passenger—Train Cars		10,539.44		65,581.52
540 Rent for Work Equipment		4.90		624.68
541 Joint Facility Rents		77,327.15		390,853.90
Total Rents Payable		199,217.00		1,043,974.09
Net Rents	(Dr.)	135,482.24	(Dr.)	732,410.03
Net Railway Operating Income		1,584,453.61		7,054,146.44

[fol. 732]

Income Statement—Concluded

	Month of May, 1943	Five Months
Other Income:		
509 Income from Lease of Road and Equipment	48.46	660.18
510 Miscellaneous Rent Income	10,644.07	37,926.59
511 Miscellaneous Non-Operating Physical Property		140.00
512 Separately Operated Properties—Profit	610.39	2,081.04
514 Income from Funded Securities	975.34	79,059.62
515 Income from Unfunded Securities and Accounts		406.71
517 Release of Premiums on Funded Debt	176.84	889.08
519 Miscellaneous Income	275.00	797.20
Total Other Income	12,730.10	121,960.42
Total Income	1,597,183.71	7,176,106.86
Miscellaneous Deductions from Income:		
543 Miscellaneous Rents	41.67	210.35
551 Miscellaneous Income Charges	281.86	444.46
Total Miscellaneous Deductions	323.53	654.81
Income Available for Fixed Charges	1,596,860.18	7,175,452.05
Fixed Charges:		
542 Rent for Leased Roads and Equipment	9,392.20	46,695.08
546 Interest on Funded Debt:		
(a) Fixed Interest	472,968.45	2,361,221.11
547 Interest on Unfunded Debt	17,858.65	86,901.35
Total Fixed Charges	500,219.30	2,494,817.54
Net Income	1,096,640.88	4,680,634.51

[fol. 733]

Profit and Loss Statement

	Month of May, 1943		Five Months
Credits:			
602 Credit Balance Transferred from Income	1,096,640 88		4,680,634 51
607 Miscellaneous Credits	2,668 18	(Dr.)	26,841 51
	1,099,309 06		4,653,793 00
Debits:			
611 Debit Balance, January 1, 1943			18,676,769 27
621 Miscellaneous Debits	298 36		20,909 86
786 Earned Surplus May 31, 1943, carried to General Balance Sheet	1,099,010 70	(Dr.)	*14,043,886 13*
	1,099,309 06		4,653,793 00

Certified as correct this 6th day of July, 1943.

T. A. Thompson, General Auditor.

Filed United States District Court, Denver, Colorado—July 7, 1943. G. Walter Bowman, Clerk.

[fol. 734] PETITION OF CITY BANK FARMERS TRUST COMPANY, FILED BEFORE THE INTERSTATE COMMERCE COMMISSION ON AUGUST 21, 1942

The petitioner admits that the present excellent earnings are unprecedented and may not continue, and that they are perhaps in part the result of the extraordinary war traffic over the lines of the Debtor.

Filed United States District Court Denver, Colorado, Sep. 30, 1942. G. Walter Bowman, Clerk.

[fol. 735] BEFORE THE INTERSTATE COMMERCE COMMISSION

PETITION OF THE DEBTOR FOR A FURTHER HEARING HEREIN FOR THE INTRODUCTION OF EVIDENCE OF CHANGED ECONOMIC CONDITIONS REQUIRING A REDETERMINATION OF THE VALUE OF THE DEBTOR'S PROPERTIES FOR PURPOSES OF REORGANIZATION UNDER SECTION 77 OF THE NATIONAL BANKRUPTCY ACT

The Denver and Rio Grande Western Railroad Company, Debtor herein, pursuant to the provisions of Section 77 of the National Bankruptcy Act and in discharge of its duties and responsibilities as therein defined, respectfully presents this Petition to the Interstate Commerce Commission for the purposes herein set forth and for the reasons herein given:

The Debtor hereby moves the Interstate Commerce Commission to rehear the issues involved in the Plan of Reorganization promulgated and approved by the Interstate Commerce Commission July 13, 1942, to the end that this Commission may give full consideration to evidence as to the extent to which the Debtor's plant has been utilized as a transportation unit and a facility in interstate commerce since the last hearing held herein by this Commission, and evidence as to the volume and character of its traffic, its revenues, its income, its operating efficiency and the consequent demonstration of earning power developed since said last hearing and may give full consideration to operating economies and efficiencies growing out of recent advances in the art of transportation which it is now possible to [fol. 736] demonstrate as attributable to property improvements and new operating methods—a demonstration which

the volume of service makes possible on the basis of actualities without the necessity as heretofore of mere estimates and conjectures—and may give full consideration to the probabilities that other National needs for the Debtor's transportation facilities and service, different in kind but not in its effect upon the volume of business and value of the service, will follow the termination of the War to the end that the factor of the Debtor's potential earning power can be given true and proper weight in the fixing of the capitalization of the reorganized structure and the distribution of its securities to the various classes of its creditors and stockholders.

The Debtor, if afforded an opportunity so to do by this Commission, is prepared to show by evidence which it believes will prove to be of a most convincing character that since the close of the hearings in this Commission and on the basis of its earnings experience since the closing of the hearing in this Commission a greatly increased earning power has been developed, much of which is in no way connected with the War or the War economy and is so far of a permanent and durable nature that it could not properly be ignored in an appraisal of the Debtor's properties and earning power for the purposes of said Section 77 and that such permanent improvement in earning power will continue even though the War demands for its services be not followed by the equal demand resulting from greatly changed necessities of the transportation business of the Nation.

Respectfully submitted, The Denver and Rio Grande Western Railroad Company, by Michael J. Curry, Vice-President.

Dated, New York, N. Y., April 30, 1943.
F. C. Nicodemus, Jr., William V. Hodges, of Counsel.

[fols. 737-738] *Duly sworn to by Michael J. Curry. Jurat omitted in printing.*

Filed United States District Court, Denver, Colorado, Jul. 31, 1943. G. Walter Bowman, Clerk.

[fol. 739] At a General Session of the Interstate Commerce Commission, held at its office in Washington, D. C., on the 14th day of June, A. D. 1943.

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

ORDER

Upon consideration of the record in the above-entitled proceeding and the petition filed on May 1, 1943, by The Denver and Rio Grande Western Railroad Company, debtor, requesting that the proceeding be reopened for further hearing and the introduction of additional evidence pertaining to the economic conditions now existing and the prospective earnings of the new property, as they might affect the capitalization of the new company, the value of the property, and other elements of the plan of reorganization for the debtor under the provisions of section 77 of the Bankruptcy Act, as amended;

It appearing, That the petitioner has served copies of its petition upon all parties of record and no replies have been filed;

It further appearing, That petitions for modification of the plan of reorganization for the debtor, approved by report and order of this Commission dated July 13, 1942, have been filed and are pending; and

It further appearing, That additional evidence of the nature referred to in the debtor's petition filed on May 1, 1943, is not required for a determination of the mat- [fol. 740] ters involved in a further modification of the aforesaid plan of July 13, 1942;

It is ordered, That said petition be, and it is hereby, denied.

By the commission,

W. P. Bartel, Secretary. (Seal.)

Filed United States District Court, Denver, Colorado. June 28, 1943. G. Walter Bowman, Clerk.

[fol. 741] At a General Session of the Interstate Commerce Commission, held at its office in Washington, D. C., on the 6th day of September, A. D. 1943.

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY
REORGANIZATION

ORDER

Upon consideration of the record in the above-entitled proceeding and the pleading entitled "Exceptions" and "Petition for reconsideration," filed on July 12, 1943, by The Denver and Rio Grande Western Railroad Company, debtor, demanding that the Commission rescind its third supplemental report dated June 14, 1943, further modifying and approving a plan of reorganization, and the orders made and filed therewith, that the Commission rescind its action of the same date denying the debtor's petition requesting that the proceedings be reopened for further hearing to permit the introduction of additional evidence, and that the Commission now set this proceeding down for further hearing; and

It appearing, That the petitioner has served copies of its petition upon all parties of record and no replies have been filed with the Commission; and

It further appearing, That the petitioner has not shown any reasons for the requested action other than those which were before the Commission for its consideration at the time of the issuance of the aforesaid report and orders of June 14, 1943:

It is ordered, That the debtor's above-described petition be, and it is hereby, denied.

By the Commission.

A true copy:

W. P. Bartel, Secretary of the Interstate Commerce Commission. (Seal.)

Filed United States District Court, Denver, Colorado; Sep. 22, 1943. G. Walter Bowman, Clerk.

[fol. 742] IN UNITED STATES DISTRICT COURT

OBJECTIONS OF THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, THE DEBTOR HEREIN, AND ITS SUBSIDIARY COMPANIES, TO THE PLAN OF REORGANIZATION CERTIFIED TO THE COURT BY THE INTERSTATE COMMERCE COMMISSION AS MODIFIED AND APPROVED BY ITS THIRD SUPPLEMENTAL REPORT AND ORDER DATED JUNE 14, 1943, AND STATEMENT OF THE DEBTOR'S CLAIM FOR EQUITABLE TREATMENT.

The Denver and Rio Grande Western Railroad Company, the Debtor herein, on its own behalf and on behalf of The Denver and Salt Lake Western Railroad Company and The Rio Grande Junction Railway Company (each of which last named companies unites herein) and (to the extent that it lawfully may) also on behalf of Goshen Valley Railroad Company and The Denver and Salt Lake Railway Company, of each of which it is the owner of not less than 91.78% of its outstanding capital stock, hereby objects to the Plan of Reorganization certified to this Court by the Interstate Commerce Commission, as modified and approved by its Third Supplemental Report and Order dated June 14, 1943 (hereinafter called "Reorganization Plan"), and in accordance with subsection (e) of Section 77 of the Act of Congress commonly known as the National Bankruptcy Act, and pursuant to order of this Court, No. 463, filed herein on July 2, 1943, the Debtor, for itself and for said subsidiary companies, hereby presents a statement in detail of its Objections to said Plan of Reorganization and its claim for equitable treatment.

Whenever herein reference is made to the Debtor or the [fol. 743] Debtor's property or the value thereof, such reference, unless the context shows otherwise, shall be deemed to include the property or the value of the property of the Debtor and its aforesaid subsidiary companies.

In limine the Debtor objects to any consideration by the District Court of the Plan of Reorganization certified as aforesaid to the Court by the Interstate Commerce Commission on the ground that the Commission's determination was made without a hearing of the character required by the Fifth Amendment to the Constitution of the United States and is in effect an attempt to take the Debtor's property without due process of law and without observing the

process as provided by Section 77 of the National Bankruptcy Act.

Specifically the Debtor excepts to and objects to a denial of the Debtor's petition filed with the Commission on May 1, 1943, a copy of which is hereto annexed and made a part hereof; and the Debtor hereby moves for an order by this Court referring this proceeding back to the Interstate Commerce Commission to receive evidence of the character outlined therein and for proceedings in accordance with the Statutes of the United States.

Subject to the aforesaid reservation of its constitutional rights and without a waiver thereof the Debtor states the following Objections to the Plan so certified to this Court by the Interstate Commerce Commission and the following claim for equitable treatment:

A. Objections to the Plan of Reorganization Certified to this Court by the Interstate Commerce Commission, as Modified and Approved by Its Third Supplemental Report and Order Dated June 14, 1943.

1. The Debtor renews all of its Objections to the Plan of Reorganization promulgated by the Interstate Commerce Commission on April 2, 1940, which Objections were filed with the District Court on July 1, 1940, except to the ex-
[fol. 744] tent that said Objections are given recognition by the Third Supplemental Report and Order of the Interstate Commerce Commission dated June 14, 1943, to which these Objections relate.

2. The Debtor specifically objects to the findings of the Commission as to the total capitalization of the reorganized Company and as to the value of the property of the Debtor and avers that the actual value is in excess of the total capitalization as found by the Commission in the Plan of Reorganization now certified to the District Court, and that such capitalization is less than the true value of the property protected by the Fifth Amendment.

3. In addition to the recognition due to the Preferred Stock and Common Stock of the Debtor without the payment of any consideration, the Debtor submits that holders of its Preferred Stock and Common Stock should be given a preferential right on terms to be fixed to redeem proportionately the collateral proposed to be placed by

the Commission's modified Plan under the extended collateral note held by The Chase National Bank of the City of New York and that purchase warrants representing such rights should be authorized.

4. The Debtor objects to the failure of the Commission to value the shares of the capital stock of Utah Fuel Company allotted to the holders of the First Consolidated Mortgage Bonds of the Rio Grande Western Railroad Company and its failure to deduct the value thereof from the claim which it has purported to satisfy by the allocation of new securities in the reorganized Company.

B. Claim of Debtor for Equitable Treatment.

In its claim for equitable treatment the Debtor asks that the Plan of the Interstate Commerce Commission certified to the District Court as aforesaid by the Commission's Third Supplemental Report be set aside and that a new [fol. 745] Plan be certified providing for a capitalization which will make whole all of the Debtor's creditors and will provide for allotments of stock in the reorganized Company to the Debtor for the use and benefit of its shareholders as their interests may appear; and that in addition warrants be issued to the holders of the Debtor's Preferred Stock and Common Stock entitling them in the order of their respective priorities to redeem proportionately all collateral underlying the proposed extended collateral note held by The Chase National Bank of the City of New York.

Dated, July 29, 1943.

Pierce & Greer, 40 Wall Street, New York, New York; Hodges, Vidal & Goree, Equitable Building, Denver, Colorado, Attorneys for the Debtor and its above-named subsidiary companies as Objectors.

Frank C. Nicodemus, Jr., William V. Hodges of Counsel.

Filed United States District Court, Denver, Colorado, Jul. 31, 1943. G. Walter Bowman, Clerk.

[fol. 746] IN UNITED STATES DISTRICT COURT

JOINT STATEMENT BY DEBTOR AND SUBSIDIARY DEBTOR OF THE POINTS UPON WHICH THEY, AS APPELLANTS, WILL RELY ON THEIR APPEALS FROM THE ORDER OF THE COURT ENTERED OCTOBER 25, 1943.

Now come the Debtors above named and jointly and severally file their Statement of Points on which they intend to rely on their appeal from the order of this Court entered October 25, 1943, approving the Plan of Reorganization of the Debtors' properties certified to this Court by the Interstate Commerce Commission and dated June 14, 1943.

Said Points are as follows:

Point No. 1

The Plan of Reorganization approved by the Court in its order of October 25, 1943, is not fair and equitable, does not afford due recognition to the rights of each or any class of creditors and stockholders, does discriminate unfairly in favor of classes of creditors holding senior liens and as against creditors junior thereto, and does discriminate unfairly against the Debtors and their stockholders, and does not conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders in the securities of the reorganized company, all contrary to Section 77, subsection (c) of the Bankruptcy Act. The Court erred in approving said Plan.

Point No. 2

On the 14th day of April, 1943, there was pending before the Interstate Commerce Commission a proceeding in this [fol. 747] cause for the formulation of a plan of reorganization under Section 77, and on said last mentioned date, while said matter was so there pending, the Debtors filed with said Commission a petition alleging that since the closing of testimony on hearings theretofore had before the Commission on the Plan there had become available proof of an earning experience of Debtors' property which had shown a greatly increased ear-ing power, permanent and durable, not provable by facts known at or prior to the closing of the said testimony, much of which was in no way

connected with the war or the war economy, showed a permanent improvement in earning power of all Debtors' properties; and the Debtors asked that an opportunity be given to present evidence thereof to the Commission and that the same be considered by the Commission in arriving at a Plan of Reorganization. The Commission erroneously denied to the Debtors the opportunity to make such proof and give testimony concerning the same and be heard thereon and certified its Plan to the Court on or about the 14th day of June 1943 without affording the Debtors an opportunity to be heard in the presentation of such facts or in arguments concerning the pertinency thereof, and thereby, in violation of the due process clause of the Constitution, denied to the Debtors a full, free and fair hearing in support of their claim for equitable recognition. The Court erred in approving said Plan and in not ordering it returned to the Commission for a hearing of said petition and further consideration.

Point No. 3

That the Commission had not before it any competent testimony to support its alleged finding of permissible capitalization for a reorganized company owning the Debtors' assets at any level of capitalization which could equitably result in the exclusion of the principal Debtor and its stockholders from participation in the securities of the [fol. 747-A] reorganized company, nor was there such testimony in the record certified by the Commission to the Court, nor was such testimony presented to the Court. The Court erred in approving the Plan which so excluded the Debtors and their stockholders without any competent testimony on which to base findings or conclusions justifying such exclusion.

Point No. 4

That the Commission's alleged findings of capitalizable value were unsupported by competent testimony, were based upon the Commission's own opinions not given in evidence or made subject to cross-examination. The Court erred in approving the Plan based on such alleged findings.

Point No. 5

That the Commission received and considered the report of its own Bureau of Valuation covering in detail the opinion

of that Bureau as to physical values of Debtors' operating properties, that said report was not competent proof of the matters set forth therein, and the Commission denied to the Debtors the right to cross examine the employees of the Commission who were the authors of such reports and refused to strike such reports from the record; that this action by the Commission was a denial of a substantial right to a full, free and fair hearing and violated the due process provisions of the Constitution. The Court erred in approving a Plan based on a record of hearings so conducted in violation of the Debtors' right to a full, free and fair hearing.

Point No. 6

That the findings of the Commission as to the prospective future earnings of the Debtors' property was based entirely on its own opinion as to such earnings, unsupported by any sworn testimony whatsoever as to the expert opinion of any witness as to such prospective earnings. The Court erred in approving the Plan which was predicated on findings of fact supported solely by the opinion of the Commission.

[fol. 748]

Point No. 7

The Plan failed to authorize capitalization for the reorganized company at not less than the minimum for which there was support in the evidence before the Commission. The Court erred in approving the Plan and in failing to return it to the Commission for further consideration.

Point No. 8

The Plan failed to authorize the capitalization of the reorganized company of at least two hundred million dollars, as shown by the only competent testimony before the Commission or the Court. The Court erred in approving a Plan with a lower capitalization.

Point No. 9

The Court erred in approving a plan with a total capitalization of not more than $155,173,127.00.

Point No. 10

Said Plan fails to give weight to increases in the Debtors' assets accumulated during the Court's administration, and the Court erred in approving the Plan.

Point No. 11

The Plan fails to give effect to improved operating economies resulting from the large expenditures for additions and betterments made by the Trustees of the Debtors' properties during the Court's administration and the newly developed traffic and improved traffic and earnings, opportunity to give testimony and be heard concerning which was rejected by the Commission. The Court erred in approving the Plan and in not returning it to the Commission for further consideration.

Point No. 12

The Court erred in not making an independent determination of the amount of each mortgage creditor's claim on account of which such creditor should be entitled to receive securities in a reorganized company, and in not determining what part of each claim is entitled to the priority as provided in its respective mortgage.

[fol. 749] Point No. 13

The Commission failed to determine the earnings during administration of the respective items of property constituting security for each mortgage issue and failed to properly account the same and distinguish in its treatment of claims between interest which would accrue during administration at contract rates to which such earnings should be credited, and the uniform non-contract equitable interest no so earned, the allowance to which is subject to the equitable discretion of the Court, and thereby, in the Plan, made unjust and inequitable allotment of the proposed new securities in violation of the law of the land governing the administration of bankrupt estates. The Court erred in approving the same.

Point No. 14

The Commission computed interest on all secured mortgage bonds at the legal rate of interest to the effective date of the Plan and by and through its allotment of new

securities in the Plan compounded the entire amount thereof, contrary to equity. The Court erred in approving the same.

Point No. 15

The Court erred in not requiring the distribution of new securities in accordance with the rules of bankruptcy administration and distribution.

Point No. 16

The Commission erred in increasing the claim of the Rio Grande Western First Trust 4s by adding to the amount of the principal and interest due on said claim on November 1, 1935, the date when petitions for reorganization herein were filed, the accumulated contract interest subsequent to such date and awarding to the holders of said bonds a priority over securities junior in time for the amount of such accumulated interest, thereby increasing the distributive share of the Debtors' estates to which the Rio Grande Western First Trust 4s became entitled on November 1, 1935, contrary to the equitable rule of distribution in bank-[fol. 750] ruptcy. The Court erred in approving the Plan providing for such enlarged priority.

Point No. 17

The Commission erred in increasing the claim of the Rio Grande Western Consolidated 4s by adding to the amount of principal and interest due on said claim on November 1, 1935, the date when petitions for reorganization herein were filed, the accumulated contract interest subsequent to such date and awarding to the holders of said bonds a priority over securities junior in time for the amount of such accumulated interest, thereby increasing the distributive share of the Debtors' estates to which the Rio Grande Western Consolidated 4s became entitled on November 1, 1935 contrary to the equitable rule of distribution in bankruptcy, and the Court erred in approving the Plan providing for such enlarged priority.

Point No. 18

The Commission erred in increasing the claim of the Denver and Rio Grande Consolidated 4s by adding to the amount of principal and interest due on said claim on November 1, 1935, the date when petitions for reorganiza-

tion herein were filed, the accumulated contract interest subsequent to such date and awarding to the holders of said bonds a priority over securities junior in time for the amount of such accumulated interest, thereby increasing the distributive share of the Debtors' estates to which the Denver and Rio Grande Consolidated 4s became entitled on November 1, 1935 contrary to the equitable rule of distribution in bankruptcy. The Court erred in approving the Plan providing for such enlarged priority.

Point No. 19

The Commission erred in increasing the claim of the Denver and Rio Grande Consolidated 4½s by adding to the amount of principal and interest due on said claim on November 1, 1935, the date when petitions for reorganization herein were filed, the accumulated contract interest subse-
[fol. 751] quent to such date and awarding to the holders of said bonds a priority over securities junior in time for the amount of such accumulated interest, thereby increasing the distributive share of the Debtors' estates to which the Denver and Rio Grande Consolidated 4½s became entitled on November 1, 1935 contrary to the equitable rule of distribution in bankruptcy. The Court erred in approving the Plan providing for such enlarged priority.

Point No. 20

The Commission erred in increasing the claim of the Refunding and Improvement 5s by adding to the amount of principal and interest due on said claim on November 1, 1935, the date when petitions for reorganization herein were filed, the accumulated contract interest subsequent to such date and awarding to the holders of said bonds a priority over securities junior in time for the amount of such accumulated interest, thereby increasing the distributive share of the Debtors' estates to which the Refunding and Improvement 5s became entitled on November 1, 1938 contrary to the equitable rule of distribution in bankruptcy. The Court erred in approving the Plan providing for such enlarged priority.

Point No. 21

The Commission erred in increasing the claim of the Refunding and Improvement 6s by adding to the amount of principal and interest due on said claim on November 1, 1935, the date when petitions for reorganization herein were

filed, the accumulated contract interest subsequent to such date and awarding to the holders of said bonds a priority over securities junior in time for the amount of such accumulated interest, thereby increasing the distributive share of the Debtors' estates to which the Refunding and Improvement 6s became entitled on November 1, 1935 contrary to the equitable rule of distribution in bankruptcy. The Court erred in approving the Plan providing for such enlarged priority.

[fol. 752] Point No. 22

The Commission erred in not allotting to the claim of the holders of the General Mortgage 5s securities in the reorganized company which, measured by capitalizable value of Debtors' properties properly determine, would compensate said holders in full for said claim. The Court erred in approving a Plan which did not so provide.

Point No. 23

The Court erred in approving a Plan which made an inequitable provision for the allotment to the holders of the General Mortgage 5s of a participation in the securities of the reorganized company.

Point No. 24

The Commission erred in not providing for the recognition of the Debtors in the reorganized company by an allotment of the voting stock of said company, and in not providing a voting stock for that purpose. The Court erred in approving a Plan which did not so provide.

Point No. 25

The Court and the Commission erred in not providing for the purchase by the Debtors of the stockholders of the principal Debtor of the voting stock of the reorganized company through the issue of warrants to the Debtor or its stockholders entitling them to purchase the same at a fair price and within a reasonable time as will appear to be justified after correction of the errors specified herein.

Point No. 26

The Commission allotted to the holders of Rio Grande Western Consolidated 4% bonds securities in the reor-

ganized company based on the full face amount of said bonds plus accrued interest to January 1, 1943, and allowed such bondholders to retain the stock of the Utah Fuel Company of substantial value pledged to secure their said bonds by owners other than the Debtors, without requiring that the value of the said Utah Fuel Company stock be credited on the claims of said bondholders, and limiting distribution of new securities in reorganization to said bondholders to the balance of said claim after such credit, contrary to [fol. 753] equity and the law of bankruptcy administration and distribution. The Court erred in approving said Plan and the proposed distribution of new securities to such bondholders.

Point No. 27

That the Plan as certified by the Commission provides for the allotment to the holders of Rio Grande Junction First Mortgage Bonds of approximately $2,400,000.00 of the proposed new First Mortgage Bonds, and $634,000.00 of the proposed new Income Bonds of the reorganized company; that subsequent to such certification the representatives of the holders of said bonds demanded the payment thereof as an operating obligation of the Court and the Court ordered the same purchased by the principal Debtor's Trustees and the purchase was made; that no equitable adjustment of new securities was made to give the creditors of the principal Debtor junior to said Rio Grande Junction First Mortgage Bonds securities in the reorganized company readjusted because of the elimination of the allotment to Rio Grande Junction First Mortgage Bonds proposed in said Plan. The Court erred in approving the Plan without requiring such redajustment to be made in accordance with procedures provided in Section 77.

Point No. 28

The Court erred in the recital and finding in its Order adopting the findings and the conclusion of the Commission as its own.

Point No. 29

The Court erred in approving a Plan which provides that the stock of the reorganized company, preferred and common, shall be par value stock, and in not providing for non par voting stock.

Point No. 30

The Court erred in approving a Plan which fails to recognize the duty of the principal Debtor under Section 77 to carry out the Plan.

[fol 754] Point No. 31

The Court erred in approving a Plan which provides for a reorganization committee and charges it with the duty of carrying out the Plan.

Point No. 32

The Commission exceeded the powers given it under Section 77 in attempting to limit the capitalization of the new company below the net investment of the principal Debtor in used and usable property. The Court erred in approving the action of the Commission in so doing.

Point No. 33

In the formulation of a Plan certified by the Commission to the Court and approved by the Court, the Commission exceeded the power and authority given it by Section 77 of the Bankruptcy Laws. The Court erred in approving a Plan so certified.

Point No. 34

That said Plan is, in effect, an order confiscating the property of the Debtors and each of them, purportedly in the interest of the public, without just compensation to the Debtors or either of them, and without due process of law, all in violation of the Fourth and Fourteenth Amendments to the Constitution of the United States. The Court erred in approving said Plan.

Point No. 35

By said Plan the Commission exercised powers and authorities not vested in it by the Constitution and laws of the United States and usurped powers not given it by Congress by virtue of Section 77 of the Bankruptcy Act or any other statute, all to the injury of the Debtors and each of them. The Court erred in approving the Plan.

Point No. 36

In and by said Plan the Commission wholly ignored the terms of each and every mortgage indenture securing the

principal Debtor's mortgage indebtedness and the statutes of the State of Colorado applicable thereto, and provided [fol. 755] a forfeiture of the interest of the Debtors and each of them in the assets in the hands of the Court without a full, fair, free and lawful sale in open market as provided by said indentures and the law of the land applicable thereto. The Court erred in approving said Plan.

Point No. 37

The Court erred in denying Debtors' motion for an order on the Trustees to pay the expense of certifying record herein to the Court of Appeals of the cost of printing such record in the Court of Appeals out of funds in the hands of the Trustees in this proceeding.

Point No. 38

The Commission erred in holding a hearing on the Plan on the 20th day of May, 1941, contrary to the provisions of Section 77 and in advance of the time allowed by said statute within which the Debtors were entitled to submit a new Plan after disapproval by the Court of the Commission's first Plan, and thereby denied to the Debtors the due process provided by Section 77. The Court erred in approving the final Plan predicated on such a hearing.

Point No. 39

The Court erred in denying the principal Debtor's motion to dismiss the proceeding and return the Debtor's property to it.

Dated January 15, 1944.

Wm. V. Hodges, 947 Equitable Bldg., Denver, Colorado; P. C. Nicodemus, Jr., 40 Wall Street, New York, N. Y., Attorneys for Debtors.

Hodges, Vidal & Gorsuch, 947 Equitable Bldg., Denver, Colorado; Pierce & Greer, 40 Wall St., New York, N. Y., of Counsel.

Filed United States District Court, Denver, Colorado, Jan. 17, 1944. G. Walter Bowman.

[fol. 756] In United States District Court

Order No. 478

Findings, Order and Decree

This matter having come on to be heard on the 13th day of April, A. D. 1943, upon notice to all parties, upon the Petition of the Trustee of The Denver and Salt Lake Western Railroad Company (herein called the Salt Lake Western) for Payment of Rental and other Amounts by The Denver and Rio Grande Western Railroad Company (herein called the Rio Grande), filed March 25, 1936, as amended April 27, 1936, and upon the "Supplemental Petition for Payment of Rental for Denver and Salt Lake Western Railroad Company Properties," filed February 8, 1943, and The Moffat Tunnel Improvement District having filed its Petition in Support of Petitions of the Trustee of the Salt Lake Western, and the State of Colorado having been allowed to intervene specially for the purpose of filing its answer herein, and various other parties having filed their answers herein, and the Court having heard the testimony offered in support of or opposition to the said petitions and answers, and having heard the arguments of counsel, and having taken under consideration certain questions respecting the obligations of the Debtor Rio Grande to the Salt Lake Western, for payments of [fol. 757] rental for the use of the Dotsero Cut-off; and now being fully advised in the premises, Doth Find:

1. That the operations of the Rio Grande over the lines of The Denver and Salt Lake Railway Company between Utah Junction and Bond, and over the line of the Salt Lake Western (known as the Dotsero Cut-off) between Bond and Dotsero, by the Trustees of the Rio Grande, in accordance with the terms and provisions of the Joint Trackage Agreement dated October 15, 1928, between The Denver and Salt Lake Railway Company and the Rio Grande, and the Dotsero Cut-off Agreement, dated June 22, 1931, between The Denver and Salt Lake Railway Company, the Salt Lake Western, and the Rio Grande, as supplemented by a certain other agreement dated December 28, 1932, evidencing a loan of $3,631,000 by Reconstruction Finance Corporation to the Rio Grande to construct the Dotsero Cut-off, modifying and fixing as provided therein, annual rental for the use of the properties of the Salt

Lake Western by the Rio Grande at five per cent (5%) per annum on the principal sum of $3,631,000, have been and are (in view of the provisions of the succeeding finding 3) compatible with the public interest and for the benefit and advantage of the estate of the debtor, and said contracts should be ratified, approved and affirmed.

2. That subject to the next succeeding finding 3, the payments required and the performance of the other obligations by the Rio Grande under the said Joint Trackage Agreement dated October 15, 1928, and in the said Dotsero Cut-off Agreement dated June 22, 1931, as supplemented and modified by the said agreement dated December 28, 1932, do not constitute an undue or unreasonable burden upon the estate of the debtor.

3. That the aforesaid Dotsero Cut-off agreement dated June 22, 1931, as supplemented and modified by the agreement dated December 28, 1932, or the so-called stock purchase loan agreement of December 19, 1934, between Reconstruction Finance Corporation, the Salt Lake Western, and [fol. 758] the Rio Grande do not obligate the Rio Grande or its Trustees, to pay as rental for use of the Dotsero Cut-off either (a) the interest or principal obligations of the Salt Lake Western, or the Rio Grande, under said stock purchase loan agreement of December 19, 1934, or the notes issued thereunder, or (b) the federal or state income taxes, excess profits taxes, or other taxes based upon income, of the Salt Lake Western.

4. That to and including December 31, 1942, there is due and owing as an administrative claim from the Rio Grande and its Trustees to the Trustee of the Salt Lake Western, accrued and unpaid rental for the use of the properties of the Salt Lake Western by the Rio Grande and its Trustees, at the rate above specified, $1,352,589.75, without interest, according to the terms and provisions of the said Dotsero Cut-off Agreement dated June 22, 1931, as supplemented and modified by the said agreement dated December 28, 1932.

Wherefore, It Is Ordered and Decreed:

1. That the Joint Trackage Agreement between The Denver and Salt Lake Railway Company and the Rio Grande, dated October 15, 1928, and the Dotsero Cut-off Agreement between The Denver and Salt Lake Railway Company, the

Salt Lake Western, and the Rio Grande, dated June 22, 1931, as modified by a subsequent agreement between the Rio Grande and Reconstruction Finance Corporation, fixing as therein provided, the rental at five per cent (5%) per annum on $3,631,000, be ratified, approved and affirmed according to their terms.

2. That pursuant to the aforesaid finding 3, the Rio Grande or its Trustees are not obligated to pay to the Salt Lake Western as rental for use of the Dotsero Cut-off either (a) the interest or principal obligations of the Salt Lake Western, or the Rio Grande, under said stock purchase loan agreement of December 19, 1934, or the notes issued thereunder, or (b) the federal or state income taxes, excess profits taxes, or other taxes based upon income, of the Salt Lake Western.

3. That the Trustees of the debtor Rio Grande shall per- [fol. 759] form and continue to perform the obligations of the Rio Grande contained in said agreements, according to their terms as modified and as herein determined, and shall pay forthwith to the Trustee of the Salt Lake Western the sum of $1,352,589.75, without interest, as the full amount of rental for the use and operation of the properties of the Salt Lake Western by the Rio Grande or its Trustees, through December 31, 1942, and that in the future, until further order of the court, the Trustees of the Rio Grande shall pay to H. Allyn Hicks, Jr. as Trustee of the Salt Lake Western, as rental for the use of its properties, such amounts, when due, as are provided in the said Dotsero Cut-off Agreement, according to its terms, as supplemented and modified by the said agreement dated December 28, 1932, said rental being at the rate of five per cent (5%) per annum on the principal sum of $3,631,000, such sums so paid to be held by the said Trustee of the Salt Lake Western, for such disposition as may later be ordered by the court.

Dated at Denver, Colorado, this 13 day of Sept., A. D. 1943.

By the Court:

J. Foster Symes, Judge.

Filed United States District Court, Denver, Colorado, Sep. 13, 1943. G. Walter Bowman.

Entered on the docket September 13, 1943.

[fol. 760] IN UNITED STATES DISTRICT COURT

ORDER

On Petition of Insurance Group Committee, Certain Indenture Trustees, and Reconstruction Finance Corporation for Payment of Interest

The petition of

Insurance Group Committee, representing certain Institutional Owners of certain Rio Grande Western Railway Company First Trust 4's due 1939 (the bonds of such issue being hereinafter sometimes called the Trusts), Denver & Rio Grande Railroad Company Consolidated 4's and 4½'s due 1936 (the bonds of such issue being hereinafter sometimes called the Eastern Consols), Rio Grande Western Railroad Company Consolidated 4's due 1949 (the bonds of such issue being hereinafter sometimes called the Western Consols),

Central Hanover Bank and Trust Company, as Trustee for the Trusts,

United States Trust Company, of New York, as Trustee for the Eastern Consols,

Guaranty Trust Company of New York, as Trustee for the Western Consols,

The Chase National Bank of the City of New York, as Trustee for the Debtor's Refunding and Improvement Mortgage 5's due 1978 and 6's due 1974 (the bonds of such issues being hereinafter sometimes called the R & I's), and

Reconstruction Finance Corporation (hereinafter sometimes called RFC)

requesting that the Debtor's Trustees be authorized to make [fol. 761] an immediate payment of overdue interest on the above bonds outstanding or held in pledge having been considered by the Court, and the Court having heard testimony in that regard and being fully advised in the premises,

It is ordered:

1. That the Debtor's Trustees be, and they hereby are, authorized and directed to pay, at a date, as soon as reasonably feasible, to be determined by such Trustees, the aggregate amount of $2,398,679.11 on the following bonds in the following respective amounts as payments of or on account of the following respective instalments of interest:

(a) $54.55 on each $1000 bond of the Trusts outstanding or pledged to be applied to the payment in full of interest

thereon for the year 1943 at the rate of 4% per annum and on account for the interest thereon for the year 1942;

(b) $22.53 on each $1000 4% bond of the Eastern Consols outstanding or pledged to be applied to payment on account of interest thereon for the year 1943;

(c) $23.24 on each $1000 4½% bond of the Eastern Consols, outstanding or pledged to be applied to payment on account of interest thereon for the year 1943;

(d) $11.97 on each $1000 bond of the Western Consols outstanding or pledged, to be applied to payment on account of the instalment of interest due October 1, 1943;

(e) $17.18 on each $1000 5% bond of the R & I's outstanding or pledged, to be applied to payment on account [fol. 762] of the instalment of interest due October 1, 1943;

(f) $18.10 on each $1000 6% bond of the R & I's outstanding or pledged to be applied to payment on account of the instalment of interest due October 1, 1943;

2. That upon the consummation of any plan of reorganization in these proceedings with an effective date earlier than January 1, 1944, the total amounts of interest by this Order directed to be paid in respect of issues of existing securities shall, subject to further order of this Court, be credited against the unpaid fixed interest and contingent interest accrued or to accrue for the year 1943 upon the new securities to be issued under such plan in exchange for such respective issues of existing securities, the Court reserving, however, full power to direct other treatment of such payment in any case where the foregoing provision shall not be appropriate.

3. That each of the payments provided for in paragraph 1 of this Order shall be made only at such office or offices as the Debtor's Trustees may designate in the City of New York, New York, and at the office of the Debtor's Trustees in the City of Denver, Colorado, upon presentation of the bonds of the respective issues to be stamped with a legend substantially as follows:

> $—— has been paid on this bond pursuant to Order No. — of the United States District Court for the District of Colorado in proceedings entitled 'In the

Matter of The Denver & Rio Grande Western Railroad Company, Debtor' No. 8669, in payment of

If and when any plan of reorganization with an effective date earlier than January 1, 1944 shall be consummated in said proceedings, such payment shall, subject to further order of said Court, be credited against the fixed interest, prior contingent interest and con-[fol. 763] tingent interest accrued or to accrue in respect of the year 1943 upon the securities which may be exchanged for this bond under such plan."

4. That coupon bonds of the Western Consols presented for payment as herein provided shall have the coupons due April 1, 1935, and all subsequent coupons attached, and coupon bonds of the R&I's presented for payment as herein provided shall have the coupons due April 1, 1935, and all subsequent coupons attached.

5. That the Debtor's Trustees be, and they hereby are, authorized and directed to return the bonds presented to them for payment pursuant hereto, stamped with the appropriate legend referred to in Paragraph 3 hereof, to the person or persons entitled to receive the same.

6. That the interest paid as herein provided on pledged bonds be applied by the pledgees thereof to the latest instalments of interest due in respect of periods prior to January 1, 1944 on the obligations of the Debtor secured by such pledge.

7. That no interest upon overdue interest paid pursuant hereto shall be paid and that acceptance of any payment of interest authorized or directed by this Order by any person authorized or entitled to receive such payment shall constitute a waiver of interest upon the interest so paid.

8. That, if any payments made in accordance with the terms of this Order prove to be in excess of the amounts properly payable, appropriate adjustment shall hereafter be made with regard thereto in such manner as the Court [fol. 764] shall deem equitable; and if any payments made in accordance with the terms of this Order prove to be less than the amounts properly payable, supplemental payments shall be made with regard thereto in such manner as the Court shall deem equitable; and the Court reserves full jurisdiction to make such readjustments; the present Order

of distribution not being designed to constitute an adjudication of relative rights.

9. That the application of all sums authorized to be paid by this Order to the respective instalments of interest specified in this Order shall not be construed in any wise as a release or waiver of the respective claims for unpaid interest due prior thereto.

10. That the Debtor's Trustees be, and they hereby are, authorized and directed to place the above sums in separate accounts for the purposes of this Order only, to take such other action as may be necessary or appropriate to carry out its provisions and to pay the normal United States Income Tax, if any, on the respective portions of said interest instalments to the extent provided by the terms of the respective mortgages.

11. That no security holder or other party to these proceedings shall be prejudiced by this Order in respect of any questions material to the formulation of a plan of reorganization or the approval or confirmation thereof.

J. Foster Symes, District Judge.

Dated April 27th, 1944.

Filed United States District Court, Denver, Colorado Apr 27 1944—G. Walter Bowman, Clerk.

Entered on the Docket April 27, 1944.

[fol. 765]. In United States District Court

Petition of City Bank Farmers Trust Company, as Trustee of the General Mortgage, for Construction of the Plan and for Other Relief, and Supporting Memorandum.

City Bank Farmers Trust Company, as trustee under the General Mortgage dated February 1, 1924, of The Denver and Rio Grande Western Railroad Company, respectfully alleges as follows:

1. The Interstate Commerce Commission's Third Supplemental Report and Order (hereinafter called the "ICC Report"), dated as of June 14, 1943, sets forth a modified

reorganization plan (hereinafter called the "Plan") for the Debtor.

2. The Plan provides for a capitaliaztion of the reorganized corporation of $155,173,127.*

[fol. 766] 3. The effective date of the Plan is January 1, 1943. The ICC Report and the Plan are based on figures as of that date.

4. The authorized capitalization includes $4,354,816 of new common stock to provide a 10% distribution on the claim of the General Mortgage Bondholders, which, as of January 1, 1943, aggregated $43,548,155.

5. The authorized capitalization as set forth in the ICC Report included $2,123,918 of new First Mortgage Bonds and $634,417 of new Income Mortgage Bonds to provide a 100% distribution on the claim of the Rio Grande Junction Bonds (hereinafter called the "Junction Bonds"), which, as of January 1, 1943, aggregated $2,758,333. Thus, approximately 2¾ millions of new senior securities were to be used under the Plan to satisfy the claim of the Junction Bondholders.

6. Upon information and belief, the payment or purchase of the Junction Bonds pursuant to the order of this Court did not deplete the Debtor's cash, current assets or excess of current assets over current liabilities to a point below that which existed as of January 1, 1943.

7. The ICC Report provides (at page 24 of the mimeographed order):

> "The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively."

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* For convenience, the figures used are those provided on the basis of consolidation of the Debtor with the Denver & Salt Lake. Either or both sets of figures could, of course, be used equally well.

The ICC Report further provides (at page 19 of the mimeographed order):

> "In view of possible changes in the amounts of the obligations herein shown as outstanding, the [fol. 767] reorganization committee shall be authorized, in order to give effect to such changes, to make such adjustments in the claims provided for in the plan, and such changes in allotment of securities, consistent with the provisions of the plan, as may be approved by the court."

8. Pursuant to the provisions of the ICC Report this Court may, either acting alone or with the reorganization committee, make such changes in the allotment of securities, consistent with the provision of the Plan, as may be equitable in the light of material changes occurring since the Plan came forward including changes in the amount of the Debtor's obligations outstanding as a result of the payment or purchase of the Junction Bonds.

9. In the event this Court should conclude that it does not possess the power, either acting alone or with the reorganization committee, to make such changes, this Court should refer the matter to the Interstate Commerce Commission for a supplemental report and order.

10. Unless approximately 2¾ millions of securities (in addition to the $4,354,816 of new common stock presently allotted to the General Mortgage issue) are allotted to the holders of the General Mortgage Bonds, the Plan will fail to conform in one of its vital details to the Plan as certified by the Commission.

11. It is necessary that this Court should interpret the Plan, as affected by the purchase or payment of the Junction Bonds, and determine what revised disposition should be made of the $155,173,127 authorized capitalization in the light of the material changes occurring since the Plan came forward.

[fol. 768] Wherefore the General Mortgage Trustee respectfully prays:

That this Court enter its order

(A) interpreting the Plan, as affected by the purchase or payment of the Junction Bonds, and providing for the

allocation to the General Mortgage issue of additional securities approximately equal in principal or par amount to the principal amount of the securities which are included within the approved capitalization and which should, as a result, be otherwise distributed, or

(B) directing the reorganization committee to make such changes in the allotment of securities, consistent with the provisions of the Plan, as may be equitable in the light of material changes occurring since the Plan came forward including changes in the amount of the Debtor's obligations outstanding as a result of the payment or purchase of the Junction Bonds and further directing the reorganization committee to allocate to the General Mortgage issue additional securities approximately equal in principal or par amount to the principal amount of the securities which are included within the approved capitalization and no longer required for distribution to holders of the Junction Bonds, or

(C) providing appropriate opportunity for suitable liaison between this Court and the Commission and permitting the Commission to file a supplemental report and order specifying what disposition should be made of the 2¾ millions unused balance of authorized capitalization, in the light of the material changes occurring since the Plan came forward; and

[fols. 769-770] That the General Mortgage Trustee have such other and further relief as to this Court seems appropriate.

March 28, 1944.

City Bank Farmers Trust Company, as Trustee of the General Mortgage, by Stewart C. Pratt, Vice President; Mitchell, Capron, Marsh, Angulo & Cooney, 20 Exchange Place, New York 5, N. Y.; Dines, Dines & Holme, First National Bank Building, Denver 2, Colorado, Attorneys for City Bank Farmers Trust Company, as trustee.

Edward E. Watts, Jr., Peter Hagner Holme, Milton J. Keegan, *Of Counsel.*

Filed, United States District Court, Denver, Colorado, Mar. 31, 1944—G. Walter Bowman, Clerk.

[fol. 771] IN UNITED STATES DISTRICT COURT

ANSWER OF INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE, AND RECONSTRUCTION FINANCE CORPORATION TO PETITION OF GENERAL MORTGAGE TRUSTEE FOR CONSTRUCTION OF THE PLAN AND FOR OTHER RELIEF.

Come now Reconstruction Finance Corporation, Insurance Group Committee, Central Hanover Bank and Trust Company, as Trustee under the First Trust Mortgage of Rio Grande Western Railway Company, United States Trust Company of New York, as Trustee under the Consolidated Mortgage of Denver and Rio Grande Railroad Company, Guaranty Trust Company of New York, as Trustee under the Consolidated Mortgage of Rio Grande Western Railway Company and The Chase National Bank of the City of New York as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company, all of which are intervenors herein (sometimes hereinafter referred to severally as the undersigned), and for their respective answers to the petition dated March 28, 1944 of City Bank Farmers Trust Company, as Trustee of the Debtor's General Mortgage, for construction of the Plan and for other relief, respectfully allege as follows:

1. The undersigned admit the allegations contained in paragraph 1.

2. The undersigned deny that the Plan provides for a capitalization of the reorganized corporation of $155,173,127 in all events.

3. The undersigned admit the allegations contained in paragraphs 3, 4 and 5, except that the principal amount of new First Mortgage Bonds provided for in the ICC Report is $2,123,916 and not $2,123,918 as alleged in said petition.

4. The undersigned deny knowledge or information sufficient to form a belief as to the allegations contained in paragraph 6 of said petition.

[fol. 772] 5. The undersigned admit the allegations contained in paragraph 7 of said petition.

6. As to the allegations contained in paragraphs 8-11, inclusive, of said petition, the undersigned allege that the same represent conclusions of law and do not constitute material allegations of fact, but in so far as the same are or may be considered as material allegations of fact, the undersigned deny the allegations contained in said paragraphs 8-11, inclusive, of said petition.

And as and for a further answer to said petition the undersigned respectfully allege as follows:

7. The plan of reorganization for the Debtor herein heretofore approved and certified to this Court by the Interstate Commerce Commission was approved by this Court by its Order dated October 25, 1943. No appeal was taken from said Order by City Bank Farmers Trust Company, as Trustee of the Debtor's General Mortgage, although the time for taking such appeal has long since elapsed.

And as and for a further answer to said petition the undersigned respectfully allege as follows:

8. On or about November 24, 1943 notices of appeal from said Order of this Court dated October 25, 1943 were filed by counsel for The Denver and Rio Grande Western Railroad Company, Debtor, and for The Denver and Salt Lake Western Railroad Company, Debtor. A statement of points on appeal and a designation of the contents of the record on appeal have been filed by said appellants, a counter-designation of contents of the record on appeal has been filed by certain of the undersigned, and the record on appeal has now been prepared by the clerk of this Court and certified to the Circuit Court of Appeals where said proceedings are now pending. The undersigned are informed and believe, and therefore allege, that this Court is without jurisdiction to consider or pass upon the matters and things referred to in said petition during the pendency of said appeals, and that in the event such jurisdiction [fol. 773] may exist this Court in its discretion should decline to consider or pass upon such matters and things during the pendency of said appeals.

And as and for a further answer to said petition the undersigned respectfully allege as follows:

9. On or about March 23, 1944 the Interstate Commerce Commission entered an order, to the full text of which the undersigned ask permission to refer on hearing with the same effect as if incorporated herein, providing for the submission of the Plan for acceptance or rejection by the creditors affected thereby, and the Plan has now been submitted to such creditors for acceptance or rejection, but said order provided that the Plan should not be submitted to the holders of The Rio Grande Junction Railway Company Bonds, and, on information and belief, the Plan has not been submitted to such holders. Under said order ballots returned to the Commission are to be postmarked not later than June 10, 1944, and it is anticipated that the Commission will certify the result of said submission to this Court at an early date.

Wherefore, the undersigned respectfully pray

(a) that said petition be dismissed on the ground that this court is without jurisdiction to consider or pass upon the same at this time,

(b) that, if considered on its merits, said petition be denied, and

(c) that the undersigned may have such other and further relief as to this Court may seem just and proper.

Respectfully submitted, Insurance Group Committee, by Hunton, Williams, Anderson, Gay & Moore, Grant, Shafroth & Toll, Their Attorneys; Central [fol. 774] Hanover Bank and Trust Company Trustee, Rio Grande Western Railroad Company First Trust 4's due 1939, by Rathbone, Perry, Kelly & Drye, Norma L. Comstock, Its Attorneys; United States Trust Company of New York, Trustee, Denver and Rio Grande Railroad Company, Consolidated 4's and 4½'s due 1936, by Stewart & Shearer, Langdon H. Larwill, Its Attorneys; Guaranty Trust Company of New York, Trustee, Rio Grande Western Railroad Company Consolidated 4's due 1949, by Davis, Polk, Wardwell, Sunderland

& Kiendl, Pershing, Bosworth, Dick & Dawson, Its Attorneys; The Chase National Bank of the City of New York, Trustee, Denver and Rio Grande Western Railroad Company Refunding and Improvement 5's due 1978 and 6's due 1974, by Milbank, Tweed & Hope, Lewis & Grant, Its Attorneys; Reconstruction Finance Corporation, by James L. Homire, Emmet McCaffery, James A. Marsh, Its Attorneys.

Filed United States District Court, Denver, Colorado, Aug. 30, 1944—G. Walter Bowman, Clerk.

[fol. 775] IN UNITED STATES DISTRICT COURT

OBJECTIONS OF CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE OF THE GENERAL MORTGAGE, TO CONFIRMATION OF PLAN OF REORGANIZATION APPROVED BY COURT'S ORDER NO. 495.

City Bank Farmers Trust Company, as Trustee under the General Mortgage, dated February 1, 1920, of The Denver and Rio Grande Western Railroad Company, asserts that the plan of reorganization (herein called the "Plan"), approved by Order No. 495 of this Court, entered on or about October 25, 1943, should not be confirmed by this Court for the reasons hereinafter set forth. It further asserts that the burden of proof rests upon any party or parties who desire that this Court should confirm the Plan, notwithstanding the adverse vote of 79.33% of the holders of the General Mortgage Bonds, to establish to the satisfaction of this Court (a) that the Plan makes adequate provision for fair and equitable treatment for the interests or claims of the holders of the General Mortgage Bonds; (b) that such rejection was not reasonably justified in the light of the respective rights and interests of those rejecting the Plan and all the relevant facts; and (c) that the Plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of subsection (c) of Section 77 of the Bankruptcy Act.

Without waiving its position with respect to the incidence of the burden of proof, it files these objections to the con-
[fol. 776] firmation of the Plan:

1. The Plan fails to make adequate provision for fair and equitable treatment for the interests and claims of the holders of the General Mortgage Bonds.

2. The rejection of the Plan by 79.33% of the holders of the Debtor's General Mortgage Bonds voting on the Plan was reasonably justified in the light of the respective rights and interests of the holders of the General Mortgage Bonds and all the relevant facts.

3. The Plan fails to conform to the requirements of clause (1) of the first paragraph of subsection (e) of Section 77 of the Bankruptcy Act.

4. The Plan is not fair and equitable to the holders of the General Mortgage Bonds, does not afford due recognition to their rights, discriminates unfairly against them and in favor of other classes of creditors and does not conform to the requirements of the law of the land regarding the participation of the various classes of creditors.

5. As a result of the purchase by the Debtor's Trustees, pursuant to the order of this Court, of the outstanding First Mortgage 5% Bonds (hereinafter called the "Junction Bonds") due on December 1, 1939, of The Rio Grande Junction Railway Company, an adjustment or change in allotment of securities, consistent with the provisions of the Plan, is required by the provisions of the Plan itself and by all applicable principles of law and equity. Before the Plan may be confirmed, provision should be made for redistribution of the authorized securities of the reorganized Debtor released through such purchase of the Junction Bonds, i. e., there should be made an adjustment or change in allotment of securities, consistent with the provisions of the Plan, to give effect to the changes which [fol. 777] have occurred in the amount of the obligations in the Plan shown as outstanding.

6. As a result of the accumulation of surplus cash in the hands of the Debtor's Trustees since the date of the promulgation of the Plan by the Commission, an adjustment or change in allotment of securities, consistent with the provisions of the Plan, is required by the provisions of the Plan itself and by all applicable principles of law and equity. Part or all of such surplus cash so accumulated should be used to reduce the amount of unpaid interest

accrued on the Debtor's securities senior to the General Mortgage Bonds, thus reducing the total amount of the claims outstanding having priority over the General Mortgage Bonds. Before the Plan may be confirmed, provision should be made for redistribution of the authorized securities of the reorganized Debtor released through such payment of accrued interest.

7. Unless provision is made for redistribution, as herein prayed, of securities authorized in the Plan released through purchase of the Junction Bonds and through the payments which should be made of accrued interest on the Debtor's securities senior to the General Mortgage Bonds, the Plan is not fair and equitable to the holders of the General Mortgage Bonds, does not afford due recognition to their rights, discriminates unfairly against them and in favor of other classes of creditors and does not conform to the requirements of the law of the land regarding the participation of the various classes of creditors.

8. Unless such provision is made for redistribution of the securities released through such purchase of the Junction Bonds the Plan will wrongfully result in a reduction in the capital structure of the reorganized Debtor to an amount substantially less than the Commission found to be proper.

[fol. 778] 9. The Plan fails to give the holders of the General Mortgage Bonds adequate or, in fact, any benefit from the surplus cash in the hands of the Debtor's Trustees on the effective date of the Plan.

10. The Plan provides for a substantial and inequitable reduction in the treatment of the holders of the General Mortgage Bonds from that provided for such holders in earlier plans, which inequitable reduction apparently results from the accumulation during the reorganization period of interest on claims senior to that of the holders of the General Mortgage Bonds, notwithstanding the fact that a substantial part or all of such interest on such senior claims was earned.

11. The Plan fails to give the holders of the General Mortgage Bonds adequate or, in fact, any benefit from

the Debtor's net income available for interest, from the expenditures made by the Debtor's Trustees in improving the property and from the substantial improvement in the Debtor's cash and current assets during the reorganization period.

12. The Plan fails to authorize the maximum capitalization justified for the reorganized Debtor.

City Bank Farmers Trust Company, as trustee as aforesaid, further alleges:

I. The Plan has been accepted by 20.67% of the holders of the General Mortgage Bonds voting and has been rejected by the holders of 79.33% of such holders.

II. The holders of General Mortgage Bonds who voted to accept the Plan constitute approximately 4.47% of the total amount of General Mortgage Bonds outstanding.

III. Upon information and belief no plan of reorganization for any railroad under Section 77 of the Bankruptcy Act has been confirmed or should be confirmed in the face of an adverse vote by a majority of those voting of the [fol. 779] creditors of any class entitled to vote upon such plan.

IV. Upon information and belief no statute has been held constitutional or should be held constitutional which by its terms requires a secured creditor of any class to surrender or exchange his claim and the security therefor and to accept something else in lieu thereof, over his objection, without at least the affirmative approval of a majority in amount of claim of creditors of such class.

V. Upon information and belief subsection (c) of Section 77 of the Bankruptcy Act should, if possible, be interpreted in such a way as will permit its being sustained as not repugnant to any constitutional principle or provision; if said subsection should be construed as permitting the confirmation of a plan of reorganization in the face of an adverse vote by a majority of those voting of any class of creditors entitled to vote on such plan, then such subsection should be declared unconstitutional and to provide for the taking of property without due process of law.

Wherefore, City Bank Farmers Trust Company, as Trustee as aforesaid, respectfully prays:

A. That the Plan be not confirmed.

B. That this Court enter an order, pursuant to Section 77(e) of the Bankruptcy Act, referring the case back to the Commission for further proceedings, including the consideration of modifications of the Plan or the proposal of new plans.

C. That in no event shall the Plan be confirmed without provision first being made for redistribution of that part of the authorized capitalization provided for in the Plan which was previously allocated for distribution to the holders of the Junction Bonds; such provision to include provision for distribution to the holders of the General Mortgage Bonds of at least an equivalent face amount of additional securities of the reorganized Debtor.

[fol. 780] D. That in no event shall the Plan be confirmed without provision first being made (a) for distribution of a substantial part or all of the surplus cash accumulated in the hands of the Debtor's Trustees since the date of the promulgation of the Plan by the Commission in reduction of the unpaid interest accrued on the Debtor's securities senior to the General Mortgage Bonds, and (b) for redistribution of that part of the authorized capitalization provided for in the Plan which was previously allocated for distribution to the holders of such senior securities on account of such unpaid interest; such provision for redistribution to include provision for distribution to the holders of the General Mortgage Bonds of at least an equivalent face amount of additional securities of the reorganized Debtor.

E. That this Court make such adjustment or change in the allotment of securities, consistent with the provisions of the Plan, or direct the reorganization committee provided for in the Plan to make such adjustment or change, as may be reasonably required to redistribute the new securities of the reorganized Debtor, authorized in the Plan, aggregating approximately $2,720,000 in face amount, which previously were to have been distributed to the holders of the Junction Bonds, which securities have become available for redistribution through changes in the amounts of the obligations in the Plan shown as outstanding.

F. That this Court make such adjustment or change by finding that pursuant to Order No. 484, entered on or about September 16, 1943, the Debtor's Trustees have, out of surplus cash from wartime earnings, purchased and now own Junction Bonds aggregating approximately $2,720,000; that by reason thereof it is no longer necessary for the reorganized Debtor to issue new first mortgage bonds or new [fol. 781] income bonds in exchange for the Junction Bonds so purchased by the Debtor's Trustees; and by directing that an adjustment or change in allotment, consistent with the provisions of the Plan, be made by making a redistribution of such excess securities.

G. That this Court order and require that further adjustments or changes in allotment of securities, consistent with the provisions of the Plan, be made so as to give benefit in an equitable manner to the holders of the General Mortgage Bonds of the additional surplus cash (including sums invested in government bonds) accumulated in the hands of the Debtor's Trustees out of wartime earnings and not reasonably needed in the operation requirements of the reorganized Debtor; that this Court make such adjustment by determining the amount of such surplus cash now on hand after deducting what is prudently necessary to meet the operation requirements of the reorganized Debtor and by ordering such surplus cash used by the Debtor's Trustees in the reduction of the accumulated interest on claims senior to the General Mortgage Bonds and by ordering a redistribution of the new securities made available by such payments or by such change in the amounts of obligations in the Plan shown as outstanding.

H. That in the event this Court is unwilling, without the approval of the Commission, to make the adjustments or changes in allotment of securities authorized in the Plan herein prayed for, this Court render its opinion that such adjustments or changes in allotment should be made and send a copy of such opinion to the Commission so that the Commission, of its own motion, may file a supplemental report and order approving such adjustments or changes.

I. That the Plan be referred back to the Commission for further proceedings so that the holders of the General Mort-

gage Bonds will not be injured by the great increase in the [fol. 782] indebtedness senior to them resulting from the accumulation of unpaid but earned interest during these proceedings and will be given the benefit of the Debtor's net income available for interest earned during these proceedings as well as the great expenditures of the Debtor's Trustees in improving Debtor's property, the improvements in cash and current asset position and the Debtor's greatly increased earnings during said period.

J. That it have such other and further relief as to this Court seems appropriate.

Dated: August 22, 1944.

Respectfully submitted, City Bank Farmers Trust Company, as Trustee as aforesaid, by Ralph E. Morton, Vice President; Mitchell, Capron, Marsh, Angulo & Cooney, 29 Exchange Place, New York 5, New York; Dines, Dines and Holme, by Peter H. Holme, First National Bank Building, Denver 2, Colorado, Attorneys for City Bank Farmers Trust Company, as Trustee as aforesaid.

Edward E. Watts, Jr., Peter H. Holme, Milton J. Keegan, of Counsel.

Filed United States District Court, Denver, Colorado, Aug. 29, 1944. G. Walter Bowman, Clerk.

[fol. 783] IN UNITED STATES DISTRICT COURT

NOTICE OF APPEAL

Notice is hereby given that City Bank Farmers Trust Company, a corporation, as Trustee Under the General Mortgage of the Debtor, one of the parties in this action, hereby appeals to the United States Circuit Court of Appeals for the Tenth Circuit, from the final Order Confirming Plan of Reorganization and final Order Denying Petition of City Bank Farmers Trust Company, as Trustee of the General Mortgage, for Construction of the Plan and for Other Relief, entered in this action on November 29, 1944,

pursuant to Memorandum Opinion on Confirmation of Plan filed in this action on November 1, 1944.

Dated at Denver, Colorado, December 15, 1944.

City Bank Farmers Trust Company, as Trustee under the General Mortgage of the Debtor, by (Sd.) Mitchell, Capron, Marsh, Angulo and Cooney.

Address: 20 Exchange Place, New York (5), New York.

(Sd.) Edward E. Watts, Jr., Dines, Dines and Holme, Peter H. Holme, Milton J. Keegan, Attorney for City Bank Farmers Trust Company, as Trustee, as aforesaid.

Address: 1210 First National Bank Building, Denver (2), Colorado.

Filed United States District Court, Denver, Colorado, Dec. 15, 1944. G. Walter Bowman, Clerk.

[fol. 784] IN UNITED STATES DISTRICT COURT

STATEMENT OF POINTS ON WHICH APPELLANT, CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE UNDER THE GENERAL MORTGAGE, INTENDS TO RELY

City Bank Farmers Trust Company, as Trustee under the Debtor's General Mortgage, dated February 1, 1924, hereby makes the following statement of points on which it intends to rely on the appeal:

1. The District Court erred in overruling and denying the objections to confirmation made by City Bank Farmers Trust Company, as Trustee.

2. The District Court erred in confirming the Plan over the rejection of the Plan by 79.33% of the holders of the General Mortgage Bonds voting on the Plan.

3. The District Court erred in holding that the Plan makes adequate provision for fair and equitable treatment for the interests or claims of the holders of the General Mortgage Bonds.

4. The District Court erred in holding that the rejection of the Plan by 79.33% of the holders of the General Mort-

gage Bonds voting on the Plan was not reasonably justified in the light of the respective rights and interests of such holders and all the relevant facts.

[fol. 785] 5. The District Court erred in holding that the Plan conforms to the requirements of clause (1) of the first paragraph of subsection (e) of Section 77 of the Bankruptcy Act; namely, in holding, in effect, that the Plan is fair and equitable, affords due recognition to the rights of the General Mortgage Bondholders, does not discriminate unfairly in favor of other classes of creditors and against the General Mortgage Bondholders, and will conform to the requirements of the law of the kind regarding the participation of the various classes of creditors and stockholders, particularly the General Mortgage Bondholders.

6. The District Court erred in construing said Section 77 as giving the Court power to confirm a Plan which had been rejected by 79.33% of the holders of the General Mortgage Bondholders voting on the Plan and in holding that, after the statutory rejection of the Plan by a class of secured creditors entitled to vote on it, the Plan could be confirmed without at least a majority vote of approval from the voting creditors of that class; such construction of Section 77 and such holding being an unwarranted and unconstitutional extension of the bankruptcy power upon which Section 77 depends for its constitutionality.

7. The District Court erred in construing said Section 77 as meaning that valuation is a function limited to the Interstate Commerce Commission which the District Court must follow, and in holding in its opinion filed November 1, 1944: "The Court in its plan of March 6, 1941, gave the General Mortgage bondholders more common stock than does the approved plan. The Commission, however, would not agree with our views, and it would seem a useless gesture for the [fol. 786] Court to make the same error again, assuming we had the power."

8. The District Court erred in holding, in effect, that said Commission in the Plan followed the statutory mandates of subsection (e) of said Section 77, which provides that the value of any property used in railroad operation

shall be determined on a basis which will give due consideration to the earning power of the property, past, present and prospective, and all other relevant facts.

9. The District Court erred in holding, in effect, that said Commission in the Plan followed the statutory mandates of subsection (e) of said Section 77, which provides that in determining the value of any property used in railroad operation, only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

10. The District Court erred in failing to hold:

(a) that when the Debtor's reorganization petition was filed in 1935, the value of the Debtor's property exceeded the amount of the claim of all holders of General Mortgage Bonds and all creditors senior to such holders;

(b) that during the reorganization period, the Debtor's net income available for interest has exceeded all Debtor's interest requirements for all securities senior to the General Mortgage Bonds, including interest on unfunded debt;

(c) that said net earned income available for interest [fol. 787] has under the law of the land been impounded for the benefit of the several classes of creditors, including the holders of the General Mortgage Bonds; and

(d) that said net earned income available for interest is still in existence, either in the form of cash and government bonds in the hands of the Debtor's Trustees or in the form of capital improvements, additions and betterments to Debtor's road and equipment;

and in failing to hold, as a result, that the Plan, which provides for the General Mortgage Bondholders new common stock equal to 10% of their claim and forfeits 90% of their claim, does not comply with the statutory mandates and the law of the land.

11. The District Court erred in denying and overruling the petition, filed herein on or about March 31, 1944, of City Bank Farmers Trust Company, as Trustee, for construction of the Plan and for other relief.

12. The District Court erred in holding, in its opinion filed November 1, 1944, that the Court had no power to make or order the reallocation of the securities authorized in the Plan and there allotted to the holders of the Rio Grande Junction 5's (bonds of the Debtor's wholly-owned subsidiary, Rio Grande Junction Railroad Company), which bonds in the meantime had been purchased by the Debtor's Trustees pursuant to the orders of the Court.

13. The District Court erred in holding that the Interstate Commerce Commission has no power to delegate [fol. 788] powers or duties to the Court and in holding that, notwithstanding the following Plan provisions:

> "In view of possible changes in the amounts of the obligations herein shown as outstanding, the reorganization committee shall be authorized, in order to give effect to such changes, to make such adjustments in the claims provided for in the plan, and such changes in allotment of securities, consistent with the provisions of the plan, as may be approved by the court",

the Court does not have the power to make the reallocation requested in said petition.

14. The District Court erred in failing to hold that the purchase by the Debtor's Trustees of said Rio Grande Junction 5's caused this senior claim, aggregating $2,758,333, to become dead to the extent that it no longer is necessary or proper to issue any of the securities authorized in the Plan in exchange therefor; and in failing to hold that all of the capitalization authorized in the Plan should be distributed to creditors.

15. The District Court erred in sustaining objection to testimony of Ralph E. Morton that it was reasonable for the General Mortgage Bondholders to vote to reject the Plan; and in failing to consider the testimony of Miles C.

Kennedy that said Bondholders were reasonably justified in voting to reject the Plan.

Dated December 19, 1944.

City Bank Farmers Trust Company, As Trustee under the General Mortgage of the Debtor, by (Sd.) Mitchell, Capron, Marsh, Angulo & Cooney.

Address: 20 Exchange Place, New York 5, New York.

[fol. 789] Edward E. Watts, Jr., Dines, Dines & Holme, Peter H. Holme, Milton J. Keegan, Attorneys for City Bank Farmers Trust Company, as Trustee, as Aforesaid.

Address: 1210 First National Bank Building, Denver 2, Colorado.

Dec. 21, 1944. G. Walter Bowman, Clerk.

[fol. 790] In United States District Court

Objections of Guy A. Thompson, Trustee in Bankruptcy of Missouri Pacific Railroad Company to Confirmation of Plan of Reorganization Approved by Court's Order No. 495.

Comes now Guy A. Thompson, Trustee in Bankruptcy of Missouri Pacific Railroad Company (hereinafter called "Missouri Pacific Trustee"), and in response to order of this Court entered the 20th day of July, 1944, setting the question of confirmation of Plan of Reorganization approved by Order No. 495 of the Court for hearing on the 30th day of August, 1944, files herein and presents to the Court his objections to the confirmation by the Court of the Plan of Reorganization of the Debtor, The Denver and Rio Grande Western Railroad Company, and the secondary Debtor, The Denver and Salt Lake Western Railroad Company, heretofore approved by the Court on the 25th day of October, 1943.

Missouri Pacific Trustee objects to the confirmation by the Court of such Plan of Reorganization (hereinafter sometimes referred to as the "Plan") for the following reasons:

1. Missouri Pacific Trustee holds title to 150,000 (50%) of the outstanding shares of the no-par common stock;

$608,000 par value of the outstanding preferred stock; and $1,000,000 of Refunding and Improvement Mortgage Bonds of The Denver and Rio Grande Western Railroad Company (sometimes referred to herein as the "debtor"); and because of such ownership, the interests of Missouri Pacific Trustee will be materially and adversely affected if the Plan should be confirmed, by reason of the fact that the Plan certified to the Court contains a finding by the Commission that the equities of the owners of the common and preferred stock of the Debtor have no value, and also contains other provisions adversely and unlawfully affecting the interests of Missouri Pacific Trustee as hereinafter set forth.

2. The Plan does not comply with the provisions of Subsection (b) of Section 77 of the Act of Congress Relating [fol. 791], to Bankruptcy, as amended, in that such Plan does not preserve the interests of the stockholders of the Debtor by providing for the issuance to such stockholders of options or warrants to receive or to subscribe for, upon fair and reasonable terms, common and preferred stock in the new or reorganized company.

3. The Commission, in finding, as set forth in the Plan, that the equities of the owners of the common and preferred stock of the Debtor have no value, and the Court in approving the Plan containing such finding, failed to give due, full, and lawful effect, and due and lawful consideration, to the value of the properties of The Denver and Rio Grande Western Railroad Company and to the earning power of such properties, past, present, and prospective, together with all relevant facts.

4. The Plan does not conform to the requirements of Clauses (1) to (3), inclusive, of the first paragraph of Subsection (e) of said Section 77, in that such Plan is unfair and inequitable, does not afford due recognition to the rights of each class of creditors and stockholders, and does not and will not conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders.

5. There has been no valuation of the properties of the Debtor such as the law requires, and the Interstate Commerce Commission is without power or jurisdiction lawfully to determine whether the equities of the owners of the com-

mon and preferred stock of said Debtor are with or without value until there has been a full and complete valuation of the properties of such Debtor; and confirmation of such Plan by this Court, absent such valuation, would be invalid.

6. The finding by the Interstate Commerce Commission that the equities of the owners of the Debtor's common and preferred stock have no value is not supported by substantial testimony and is clearly erroneous; and a confirmation [fol. 792] of the Plan by this Court would therefore be invalid.

7. The equities of the owners of the common and preferred stock of the Debtor have a substantial value; and by reason of that fact any plan is unfair and inequitable which fails to afford due recognition to the rights of such stockholders, and will not conform to the requirements of the law of the land regarding the participation of such stockholders in the Plan unless such Plan, having regard to the value of such equities, provides either for the issuance to such stockholders of stock, or options or warrants to receive or to subscribe for, upon fair and reasonable terms, common or preferred stock in the new or reorganized company.

8. The Plan does not comply with the provisions of said Sub-section (b) of said Section 77 in that, as disclosed by the testimony offered at hearings held by the Interstate Commerce Commission, a large portion of the traffic carried or which may be carried by the Debtor or by the new or reorganized company, is and will be bridge or overhead traffic, which neither originates at nor is destined to points on the lines of the Debtor. A large portion of said bridge traffic passes through the Pueblo, Colorado, gateway, the volume of which is and has been in large measure due to the fact that the Missouri Pacific Railroad Company or the Missouri Pacific Trustee, as the case may be, is a 50% owner of The Denver and Rio Grande Western Railroad Company; and unless the present measure of ownership of the Missouri Pacific Trustee in The Denver and Rio Grande Western Railroad Company is carried forward into such new or reorganized company, a long-existing and established route of trade and commerce through the Pueblo gateway, made

up of the lines of the Missouri Pacific Railroad Company and The Denver and Rio Grande Western Railroad Company, will be substantially impaired and the volume of traffic moving over such route will be substantially decreased, as the full and effective cooperation necessary to maintain such routes and cause such a large volume of [fol. 793] traffic to move thereover, can be brought about and maintained only by ownership by the Missouri Pacific Trustee in the new or reorganized Company equal to that held by such Trustee in The Denver and Rio Grande Western Railroad Company.

9. It is the opinion of the Missouri Pacific Trustee that the necessary maintenance of the Pueblo gateway can be had only through full cooperation on the part of the Debtor and those operating the properties of the Missouri Pacific Railroad Company, and that such full cooperation cannot be had unless the present ownership of the Missouri Pacific Trustee in the Debtor is carried forward in the new or reorganized company, and that, absent such ownership by Missouri Pacific Trustee in such new or reorganized company equal to the present ownership of such Trustee in the Debtor, the traffic and revenues of such new company will be so impaired that there will not be sufficient or adequate coverage of the fixed charges of the new or reorganized company; and that, by reason of the foregoing, the Plan should not be confirmed, as such Plan does not and will not comply with the provisions of Sub-section (b) of said Section 77.

10. The Plan does not provide, having regard and giving effect to the value of the equities of the owners of the common stock of the Debtor, for the issuance to Missouri Pacific Trustee of at least one-half of the common stock of the new or reorganized company, or options or warrants to receive or subscribe for, upon fair and reasonable terms, not less than one-half of the common stock of the new or reorganized company, and that such new common stock carry powers of management and control of such reorganized company; and by reason of such failure, the Plan does not conform to the requirements of Clause (1) of [fol. 794] Sub-section (e) of said Section 77.

Wherefore, Missouri Pacific Trustee respectfully prays that the Court refuse to confirm the Plan.

Dated at St. Louis, Missouri, August 26, 1944.

Guy A. Thompson, Trustee in Bankruptcy of Missouri Pacific Railroad Company, by Russell L. Diermont, H. H. Larimore, Counsel. Address of Counsel: Missouri Pacific Building, Thirteenth and Olive Streets, Saint Louis 3, Missouri.

Filed United States District Court, Denver, Colorado Aug. 28, 1944—G. Walter Bowman, Clerk.

[fol. 795] BEFORE THE INTERSTATE COMMERCE COMMISSION

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY—REORGANIZATION

Finance Docket No. 11002

Raleigh Hotel, Washington, D. C.,
Tuesday, October 20, 1936.

The above-entitled matter came on for hearing at 10 o'clock a. m., pursuant to notice.

Before Examiners R. T. Boyden and Homer H. Kirby

APPEARANCES:

Pierce & Greer, by F. C. Nicodemus, Jr., 35 Wall Street, New York City; and Hodges, Wilson & Vidal, by William V. Hodges, Equitable Building, Denver, Colorado, appearing for Denver & Rio Grande Western Railroad Company, Debtor.

Henry W. Anderson, (Hunton, Williams, Anderson, Gay & Moore, of counsel) and George D. Gibson (Hughes, Schurman & Dwight, of counsel), Electric Building, Richmond, Virginia; and Oscar R. Ewing, 100 Broadway, New York City, New York, appearing for Insurance Group Committee, [fol. 796] by George S. van Schaick, Chairman.

Harry Hoffman, 30 Pine Street, New York City, and Edgar J. Goodrich and Mildred E. Reeves, Investment

Building, Washington, D. C., appearing for Untermyer Family Group.

John B. Marsh, 20 Exchange Place, New York City, appearing for City Bank Farmer's Trust Company, Trustee of General Mortgage.

Messrs. Fred N. Oliver and Karl Michelet, 110 E. 42nd Street, Room 1313, New York City, New York, appearing for Savings Bank of Baltimore, Maryland.

Charles J. Nasmyth, 313 East 58th Street, New York City, New York, appearing for himself.

Messrs. John E. Benton and Clyde S. Bailey, 806-808 Earle Building, Washington, D. C., appearing for Public Service Commission of Utah.

Simon Fleishman, 1331 G Street, N. W., Washington, D. C., appearing for Robert R. Young, et al.

H. H. Larimore, 2008 Missouri Pacific Building, St. Louis, Missouri, appearing for Guy A. Thompson, Trustee, Missouri Pacific Railroad Company.

Russell L. Dearmont, 705 Olive Street, St. Louis, Missouri, appearing for Guy A. Thompson, Trustee, Missouri Pacific Railroad Company.

Messrs. W. Heyward Myers, Jr. and William Clarke [fol. 797] Mason, 2107 Fidelity-Philadelphia Trust Building, Philadelphia, Pennsylvania, appearing for Security Research Bureau.

Messrs. Edwin S. S. Sunderland and Thomas O'G. Fitzgibbon, 15 Broad Street, New York, New York, appearing for Guaranty Trust Company of New York as successor Trustee of the Rio Grande Western Railway Company First Consolidated Mortgage Deed, dated April 1, 1899.

Daniel Willard, Jr., Transportation Building, Washington, D. C., appearing for The Railroad Credit Corporation.

Stewart & Shearer, by Gerald Hughes, International Trust Building, Denver, Colorado, appearing for United States Trust Company of New York, Mortgage Trustee.

Henry L. Umbarger, Provident Trust Company, 17th & Chestnut Streets, Philadelphia, Pennsylvania, appearing for Provident Trust Company as unofficial observer.

Philip B. Fisher, 246 South 15th Street, Philadelphia, Pennsylvania, appearing for Security Research Bureau.

Erskine R. Myer, Midland Savings Building, Denver, Colorado, appearing for Raymond L. Sauter, Trustee of Denver & Salt Lake Western Railroad Company. (Entered by C. M. Clay of R. F. C.)

Messrs. James B. Alley, General Counsel, and C. M. Clay, Assistant General Counsel, 1825 H Street, N. W., Washing-
[fol. 798] ton, D. C., and C. C. McChord, Counsel, 714 Southern Building, 15th & H Streets, N. W., Washington, D. C., appearing for Reconstruction Finance Corporation.

Arthur A. Gammell, 15 Broad Street, New York City, New York, appearing for the Chase National Bank of the City of New York as trustee under the Denver & Rio Grande Western Railroad Company Refunding and Improvement Mortgage dated February 1, 1924.

* * * * * * *

[fol. 799] EXAMINER KIRBY:

Since the filing of the petition by the Denver & Rio Grande Western Railroad Company in the United States District Court, various documents have been filed in the proceedings in that court for reorganization of this Debtor, and copies of certain of those documents have been transmitted to the Interstate Commerce Commission, pursuant to the rules of the United States Supreme Court.

May it be understood that documents heretofore and hereafter so transmitted to this Commission and filed in this docket, constitute a part of the record in this proceeding?

Mr. Nicodemus: The Debtor so stipulates, and also stipulates that the same apply to the annual reports of the Debtor or any of its subsidiaries, filed with the Commission.

[fol. 800] Mr. Anderson: Will copies of those be furnished to the various intervenors, Mr. Examiner? Would the Debtor supply copies of those papers to the various intervenors, because otherwise we would not know what was filed, and we would have to come here and examine the records to know what was in the record, which is rather difficult.

Mr. Nicodemus: You will know what is in the record. You will get it currently.

Mr. Anderson: You mean only the printed record of the court?

Mr. Nicodemus: Yes, sir.

Mr. Anderson: Any other documents, outside of the printed record of the court, can you not supply us with copies?

Mr. Nicodemus: The stipulation does not cover anything outside the printed record of the court.

Mr. Anderson: If it is in the printed record of the court, we get copies of that. If it is the annual report of the company, and not in the printed record of the court, will you furnish us copies of those?

Mr. Nicodemus: We cannot undertake to furnish the annual reports which we file with the Commission.

Mr. Anderson: We may ask you to furnish us copies of the annual reports as printed.

Mr. Nicodemus: We probably would.

[fol. 801] Mr. Anderson: I only want to be sure that we know what is going into this record.

Examiner Kirby: Mr. Nicodemus, with respect to the annual reports of the Debtors or the carriers to the Commission, I do not believe we should stipulate or incorporate by reference in a general manner all the annual reports in the record of this proceeding. Where the occasion arises for specific schedules to be referred to, we concede the situation as it arises.

Mr. Nicodemus: Very well. That is quite satisfactory.

* * * * * * *

[fol. 802] William Wyer was sworn and testified as follows:

Direct examination.

By Mr. Nicodemus:

Q. Mr. Wyer, will you state your full name and occupation to the Examiners?

A. William Wyer, secretary and treasurer of the Missouri Pacific Railroad Company and special representative of the Denver & Rio Grande Western Railroad Company in connection with plans for reorganization.

* * * * * * *

[fol. 803] By Mr. Nicodemus:

Q. Mr. Wyer, have you prepared, or caused to be prepared, a mortgage map of the Denver & Rio Grande Western Railroad Company and its subsidiary and affiliated companies?

A. Yes, I have.

Q. Has that map been distributed among counsel and intervenors?

A. Yes.

Q. Have you any explantory statement to make respecting it, before I offer it in evidence?

A. This is not only a mortgage map but combines several purposes in one map. It shows all the lines of the different companies, and it also shows the connecting rail- [fol. 804] roads at all points of connection. It shows the liens of the different mortgages, and it shows the operating divisions into which the company is divided for operating purposes.

I would like to point out the important features of each of those points on this map, because this is the only map of the entire system which will be presented. First I will point out the lines owned by the different companies, and I will point out the subsidiaries, and the balance will be lines owned by the parent company, the Denver & Rio Grande Western.

The Denver & Salt Lake owns the line starting at Denver, in the northeast corner of the map, and extending west through the Moffat Tunnel to Orestod, and then north from Orestod to Steamboat Springs and west to Craig.

The Denver & Salt Lake Western owns the line extending from Orestod, on the Denver & Salt Lake, west and a little south to Dotsero. The Rio Grande Junction Railway Junction Company owns the line extending from Rifle, which is directly west of Dotsero, west and a little south to Grand Junction.

The Goshen Valley, the fourth subsidiary, is located in Utah, south and a little west of Utah Lake, extending from a point designated as Pearl Junction to Dividend and Iron King, which is a small branch line.

[fol. 805] The remainder of the lines shown in heavy delineations on this map are owned by the Denver & Rio Grande Western Railroad Company or are operated under trackage rights by them. The trackage rights are practically negligible.

As to important connections:

At Denver the important connections are the Union Pacific to the East and North and the Burlington to the East, the Rock Island to the East. The Rock Island uses the Union Pacific into Denver from Limon, shown right near the edge of the map, a little southeast of Denver, and the Colorado & Southern which runs north out of Denver

and also south to Colorado Springs, although that line is not shown on this map.

Also the Santa Fe connects with the lines at Denver, running south from that point to Colorado Springs.

The lines of the Santa Fe and the Denver & Rio Grande Western, between a point just south of Denver and a point just north of Pueblo, are used jointly by those two companies and by the Colorado & Southern as a paired track.

So that the line of the Santa Fe, also used by the Colorado & Southern, is not shown on this map because it is really exactly the same line as used by the Denver & Rio Grande Western.

[fol. 806] At Colorado Springs the principal connection is the Rock Island to the East.

At Pueblo, south of Colorado Springs, the principal connections are the Missouri Pacific to the East, the Santa Fe to the East, and the Colorado & Southern Line, which continues on to the South.

Between Pueblo and Walsenburg, which is about 50 miles south of Pueblo, the Colorado & Southern Line and the Denver & Rio Grande Western Line are used as a joint double track by those two properties, so that that line is not shown separately.

At Trinidad, the southeast corner of the State of Colorado, connection is made with the Santa Fe and the Colorado & Southern. The Santa Fe's main line to California passes through Trinidad, and the Colorado & Southern extends southeast into Texas from that point.

There are a number of short lines in the State of Colorado and the State of Utah which I shall not mention. They are shown, the connections are shown on the map, but the only other important connections are on the West at the Utah common points. At Ogden, in the northwest corner of the map, connection is made with the Southern Pacific, which extends west from that point; with the Union Pacific which extends north and northwest, and also to the east, and the Union Pacific also has a line between Ogden, [fol. 807] Salt Lake City, and Provo, which practically parallels the line of the Denver & Rio Grande Western.

At Salt Lake City the principal connections are the Western Pacific to the west, and the Union Pacific, which is shown on this map by its predecessor name, the San Pedro, Los Angeles & Salt Lake, which extends to the southwest. The San Pedro Los Angeles & Salt Lake, one of its prede-

cessor names, was also the Los Angeles & Salt Lake, which also connects with the Denver & Rio Grande Western at Provo, from where it extends to Lynn Junction and on to the southwest.

As to mortgages, I think it would be particularly interesting to take the main line of the Denver, starting at Denver, and trace it west and follow the different mortgage liens as they lie on that main line, because that is one of the points about which this plan turns.

From Denver, as I have shown, the Denver & Salt Lake owns the line as far west as Orestod, and that line is subject to two mortgages, the first mortgage of the Denver & Salt Lake and an income mortgage which is the second mortgage on the line.

The Denver & Rio Grande Western has trackage in that territory. These mortgages will be described more in detail later as to their terms, so that I shall not do that here but just try to help you get them in mind.

[fol. 808] From Orestod to Dotsero the line is owned by the Denver & Salt Lake Western, a wholly owned subsidiary of the Denver & Rio Grande Western; and there is no mortgage on that property but the stock of that company is pledged with the Reconstruction Finance Company.

I should also say, perhaps, that the stock of the Denver & Salt Lake, to the extent that it is owned by the Denver & Rio Grande Western, which is more than 99 percent, is also pledged with the Reconstruction Finance Corporation. So that the R. F. C., in effect, holds a lien on the equity of the Denver & Rio Grande Western on the line from Denver to Dotsero.

The line from Orestod to Dotsero is what I shall refer to frequently as the Dotsero Cutoff, or the cutoff, and was built, as will be shown later in more detail, in order to shorten the distance between Denver and Salt Lake City.

Prior to the construction of that cutoff, the Denver had had to operate out of Denver south to Pueblo, west to Salida, and north through Leadville to Dotsero, and the construction of that cutoff and arrangements for use of the Denver & Salt Lake saved approximately 173 miles in that haul between Denver and Salt Lake City, and the R. F. C. assisted in the financing of that construction and has the lien on that line.

[fol. 809] South from Dotsero west to Rifle and through Glenwood Springs, the first lien is held by the Denver &

Rio Grande Railroad Company First Consolidated Mortgage. That is a mortgage of the predecessor Denver & Rio Grande Railroad Company, which owned the property prior to the 1908 consolidation.

Now, from Rifle to Grand Junction the line is owned by the Rio Grande Junction Railway Company, and there is a first mortgage, a small first mortgage, on that line, and the bonds are in the hands of the public. There is also a second mortgage, which, together with all the stock, is pledged under the refunding and improvement mortgage of the Denver & Rio Grande Western. That is a mortgage which was put on the property in 1924, following the second receivership.

From Grand Junction to Crevasse, the next station west —I think it is 18 miles—the lien is also held by the Denver & Rio Grande first and consolidated mortgage, and from Crevasse west to Ogden the first lien is held by the Rio Grande Western first trust 4's of 1939 and the second lien by the Rio Grande Western first consolidated 4's of 1949. Both of those mortgages are mortgages of the old Rio Grande Western Railway Company which owned the property prior to the 1908 consolidation.

Now, the other main line of the Denver is the old route [fol. 810] south from Denver to Pueblo and west to Salida, and up to Dotsero, and that mileage is all under the first lien of the Denver & Rio Grande Railroad Company first consolidated mortgage.

The Narrow Gauge lines, located approximately in a square around the words "Alamosa Division" which appear in the southern part of the State of Colorado, are also subject to the first lien of the D. & R. G. First Consolidated Mortgage, with the exception of one small piece on the Santa Fe Branch, right at the end of the Santa Fe Branch, which is subject to the Refunding and Improvement Mortgage, created in 1924.

Those, I think, give you the principal points about the mileage liens of the different mortgages.

The remaining point shown by this map is the division into operating divisions, of which there are four. The lines comprising the long dash and two dots separate the mileage as to operating divisions. The Pueblo Division has the eastern part of the line, the Alamosa Division has the Narrow Gauge and a small part of the Standard Gauge and the Grand Junction Division has the line from Salida.

and Orestod west to Helper in Utah, and the Salt Lake Division has the lines west of Helper.

By Mr. Nicodemus:

Q. Was this map prepared by the Engineering Department or other proper department of the Denver & Rio [fol. 811] Grande Western Railroad Company, or its trustees, in its regular course of business?

A. This was prepared especially at my request for use in this case.

Q. And you have personally scrutinized it?

A. Yes, I have.

Q. You say that it portrays with reasonable accuracy the various properties which you have mentioned in your statement?

A. I do not think there are any mistakes in it. There are none which I have been able to find out.

Mr. Nicodemus. This is offered as exhibit No. 7.

Examiner Kirby: In the absence of objection, the map which the witness has described will be received in evidence as Exhibit No. 7.

(Exhibit No. 7, Witness Wyer, received in evidence.)

* * * * * * *

[fol. 812] When we made our first studies of the cutoff, back in 1926 and 1927, we all felt at that time on the Denver & Rio Grande Western that it would take at least five years to develop the cutoff business to what you might call a normal level, considering the general levels of traffic, and we felt, and all of our figures showed very definitely, that during at least the first three years of cutoff operation the Denver & Rio Grande Western would be worse off from a net income standpoint than it would be without the cutoff.

But it seemed quite clear that as this business over the [fol. 813] cutoff was developed and the Denver & Rio Grande Western began to prove its place as a through route having a short line between Denver and Salt Lake, and being thus better able to participate in the handling of the traffic from the Pacific Coast to Chicago through Denver, that deficit would disappear, and the final result would be well worth the expense of constructing the cutoff and the expense involved in the trackage arrangement with the Denver & Salt Lake, and the expense of acquiring that stock.

The cutoff operations have turned out exactly as we had felt that they would, on the basis of our analysis. And the first year, as I will show in more detail later, the Denver & Rio Grande Western was at least $800,000 worse off because of the cutoff in that first year than it would have been without it.

The Denver & Salt Lake, however, benefited from the opening of the cutoff route, because of the rental which it collects from the Denver & Rio Grande Western for the use of its line, and the net benefit to the Denver & Salt Lake is something in excess of $400,000 a year.

So that part of the loss on the Denver & Rio Grande Western of over $800,000 shows up in the income account of the Denver & Salt Lake, of which the Denver & Rio Grande Western owns more than 99 per cent of the stock. [fol. 814] Another thing before we leave Exhibit 17-B:

As I have told you the cutoff started operations on June 15, 1934, and it so radically changed the whole operating picture and the whole earning situation of the Denver & Rio Grande Western, that back of that time your figures are not really as significant as they are since that time. In other words, we have a pretty short period with which to work, on which we could base conclusions as to the present situation.

So that we have gone back to the very beginning of the cutoff opening and have constructed some figures which I will present later in great detail, covering the twelve months ended June 30, 1935, which is the first full year of cutoff operation, excluding the first 15 days, and that is in order to deal with the period which includes the effect of this cutoff, which I have just outlined to you.

We will pay more attention to that period, the 12 months ending June 30, 1935, than we will to the calendar year periods. As a matter of fact, the net income of the Denver & Rio Grande Western during that 12-months' period was almost exactly the same as it was during the calendar year 1935. So that I feel that the analyses which we have made of that first 12-months' period can apply very well to the [fol. 815] calendar year 1935, as well.

* * * * * * * *

[fol. 816] It is estimated by the trustees that they will earn, available for interest, during the year 1936, $2,205,000. This is in spite of the fact that they expect their gross

revenues to be very substantially higher than they were in 1935. In 1935 the operating revenues of the Denver & Rio Grande Western and these same companies was $20,944,000, and they expect that to be $25,519,000, or an increase of nearly 25 per cent, a little less than that. In spite of that they expect the income available for interest to fall from $2,832,000 to $2,205,000.

The great part of that decrease in net income may be found in the increase in operating expenses. Maintenance [fol. 817] of way they expect to increase from $2,491,000 to $3,972,000. Maintenance of equipment they expect will increase from $4,861,000 to $6,235,000, and transportation expense they expect will increase from $7,146,000 to $8,624,000. These also represent very substantial increases in the ratios as far as maintenance of way and maintenance of equipment are concerned, and because of the very heavy increases in maintenance work in 1936, during the trusteeship, we do not believe that 1936 is representative in any way of the future earning power of the property.

These maintenance expenditures are, in my opinion, much higher than would be required for 1936 business by itself under normal operations. They have undertaken a very extensive rehabilitation and improvement program, and I believe that those maintenance expenditures are very much higher than would be required if that very large program was not under way at the present time. They include, or will include, very heavy expenditures for the calendar year in connection with improvement work and also very heavy increase in the ordinary maintenance work.

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[fol. 818] By Mr. Nicodemus:

Q. Mr. Wyer, we will now pass from income to traffic density. Have you available for distribution charts showing the traffic density on the lines of the Debtor and its subsidiaries?

A. Yes, I have.

Q. Will you produce the traffic density charts for the calendar year 1935?

A. I will.

Q. Is that the latest available chart?

A. Yes; it is.

Q. That covers all of the system, as I understand it?

A. Yes, it does.

Q. If you have any comments to make on the chart, we would be glad to have them in the record.

A. This is the first full calendar year after the opening of the Dotsero Cutoff, and I want to call particular attention to three or four things on it.

You will notice especially the decrease in the volume of tonnage on the main line east of Dotsero as compared with the tonnage west of Dotsero, where the traffic diverges to [fol. 819] go over the cutoff. The figures show that about 814,000 net ton miles per mile of road is the average traffic density between Grand Junction and Minturn for the whole district, and that in addition to that average there are 554,000 net ton miles per mile of road, which leave the main line at Dotsero eastbound to come in over the cutoff to Denver.

So that of your total traffic about 40 percent at present is moving over the cutoff into Denver, and about 60 percent is moving over the old line to Pueblo.

Now, that does not mean that you have had 40 percent of your traffic diverted to the cutoff, because some of the 40 per cent now moving over the cutoff represents new traffic. And in our figures as to the effect of the cutoff, which will be presented later, we have made a distinction between the new traffic and the old traffic diverted. But that shows the extent of the volume moving over the two routes at the present time.

Then I also want to call attention to the very light traffic density of the Narrow Gauge Lines.

Q. There does not seem to be any at all.

A. On most of the lines it is so light that it is less than 50,000 net ton miles per mile of road, and consequently does not carry a line on the chart, but the traffic density is expressed solely in figures. That is true of all the narrow [fol. 820] gauge lines with the exception of the line from Crested Butte, which is directly south of Dotsero, where coal originates and comes south into Gunnison, and over Marshall Pass to Mears Junction and into Salida, where it is transferred to the standard gauge.

Then there is also a fair traffic density coming from Durango, in the southwestern corner of the narrow gauge, east to Chama, then over Cumbres Pass to Antonito, and dropped at Alamosa, where it is transferred to the standard

gauge. But with those two exceptions the narrow gauge traffic is very, very light.

Q. The line to Somerset shows some?

A. Somerset is a standard gauge line.

Then I also want to point out the heavy coal traffic in Utah, which originates in and around Helper, and which you will notice increases the westbound traffic over Soldier Summit very materially.

The traffic westbound before Helper is reached averaged in 1935, 859,000 net ton miles per mile of road, and that was increased nearly 200 percent by the addition of the coal traffic from the Helper territory. That coal traffic in the Helper territory is the largest single item traffic on the road.

Q. That affects the traffic density eastbound to some ex-
[fol. 821] tent, does it not?

A. Very, very little.

Q. Helper over to Mounds?

A. Very little.

Examiner Boyden: Is the old line from Denver through Pueblo and Salida and Dotsero used now for through traffic?

The Witness: There would not be any through traffic moving that way, but would all move through the cut-off.

Examiner Boyden: All the traffic coming from Denver through Pueblo is destined to some point south of there or some point on the line between Denver and Dotsero?

The Witness: Yes, sir.

Mr. Ewing: What are the dotted lines up on the Denver & Salt Lake?

The Witness: The dotted lines up on the Denver & Salt Lake represent the Denver & Salt Lake's traffic. The solid lines represent the Denver & Rio Grande Western's traffic.

Mr. Hoffman: What do the figures represent?

The Witness: The figures represent units of 100,000 net ton miles haul per mile of road.

Mr. Hoffman: The 6.65 would be 66,500?

The Witness: It would be 665,000 net ton miles per mile
[fol. 822] of road per year.

Examiner Kirby: Is the line from Montrose to Grand Junction standard gauge?

The Witness: Yes, sir, that is standard gauge. The narrow gauge starts at Ouray, you might say, south of Montrose, comes north to Montrose, east to Gunnison, and

then includes the Crested Butte branch east to Mears Junction, including the line northeast to Salida and the Monarch branch, and south to Alamosa, and further south to Antonito, including the Santa Fe branch south of Antonito, and takes in all the line west of Antonito.

The line from Alamosa to Creede is standard guage, and there are three rails from a point north of Alamosa down through Alamosa to Antonito, so that you can load standard gauge cars in that territory and handle either standard gauge, narrow gauge cars or both in the same territory, but that takes the circumference of the narrow gauge territory.

Examiner Kirby: Is that the extent of the three-rail mileage which you just mentioned?

The Witness: The three-rail mileage is limited to that territory which I just mentioned.

Mr. Fisher: May I ask a question? These figures on the Rio Grande Junction, such as 6.29 westbound, just what does that mean?

[fol. 823] The Witness: They are in addition to the figures which are included in the shaded area, and they represent the traffic which comes in and goes off the line at Dotsero.

Mr. Fisher: They are local traffic?

The Witness: No, it is not local traffic. It is traffic handled over the cutoff which may be destined to the Pacific Coast, or it may be destined to Grand Junction, but the figures between Grand Junction and Minturn, which are included in the shaded area, represent the average traffic density between Grand Junction and Minturn, excluding the cutoff traffic, and then the extra figures shown outside the shaded area are the Dotsero Cutoff traffic in addition.

Mr. Gibson: Do I understand you to say that the only third line is at Alamosa?

The Witness: North and south of Alamosa. It extends from north of Alamosa down to Antonito.

Mr. Marsh: I do not get what the extra figures mean. Take the line between Denver and Orestod. The solid lines are the through traffic?

The Witness: Between Denver and Orestod the solid lines are the traffic of the Denver & Rio Grande Western which operate from that territory under trackage rights.

The dotted lines are the traffic of the Denver & Salt Lake. The figures in the solid line area 5.32 eastbound, for [fol. 824] example, represent the Denver & Rio Grande

Western traffic. The 6.65 represents the D. & S. L. traffic.

Mr. Marsh: I see.

The Witness: And westbound the same way.

Mr. Marsh: Then we get on to the Rio Grande Junction Line-wesfbound 6.29, which is the Denver & Rio Grande Western traffic, and 3.63 is additional traffic?

The Witness: The 6.29 represents the traffic moving through Dotsero to Minturn, and 3.63 represents the traffic coming in on the cutoff, or, rather, I should say, the 6.29 represents the westbound traffic coming from Minturn, and the 3.63 represents the traffic coming in over the cutoff.

The reason that the figures have to be shown in that way is because the wheel reports made by the conductors covering the consist of their freight trains are made in two groups. One set runs from Grand Junction to Orestod and the other set runs from Grand Junction to Minturn. So that you have two different sets of wheel reports covering that territory in there, and the statistical compilations are made separately as to the two sets of wheel reports.

Mr. Marsh: Thank you very much.

Mr. Nasmyth: From whom are the traffic rights derived? The Denver & Salt Lake?

[fol. 825] The Witness: Are you speaking now of the line between Denver and Orestod?

Mr. Nasmyth: Yes.

The Witness: The Denver & Salt Lake owns the railroad and grants trackage to the Denver & Rio Grande Western.

Mr. Nasmyth: And the heavy lines represent the trackage rights, and the dotted lines represent the Denver & Salt Lake?

The Witness: That is right.

Mr. Nasmyth: Thank you.

Mr. Hoffman: May I ask a question on the exhibit, Mr. Wyer?

The Witness: Surely.

By Mr. Hoffman:

Q. Do I correctly understand, referring to the line from Denver to Orestod, that the major portion of the Denver's traffic is westbound?

A. No, sir, the major portion of the Denver's traffic is eastbound. The major portion of the traffic on both roads is eastbound.

Q. I cannot quite see it. Is the eastbound line the one below what is designated the railroad track?

A. Yes, sir.

Q. The arrow above the railroad track points west?

A. That is right.

Q. I see. Is there any particular reason for that which [fol. 826] you know of?

A. Reason for what?

Q. Why the largest part of the traffic which goes over the cutoff should go east and the smaller part west?

A. That is the nature of the traffic. The larger part of the traffic moving over the cutoff constitutes business that originates in local territory on the D. & R. G. W., or originates at California and comes east over the Western Pacific or the Southern Pacific, and that traffic is in excess of the westbound traffic, which is quite varied, and which is handled over the cutoff.

Mr. Nicodemus: And which was true before the cutoff was built?

The Witness: It has always been true of the through traffic on the Denver & Rio Grande Western, that it has been predominantly an eastbound traffic. It is true of every transcontinental railroad.

By Mr. Hoffman:

Q. Let me ask a question. Is there any traffic which comes from the old main line of the Denver between Pueblo and Dotsero, that is routed first west and then east over the cutoff?

A. There might possibly be, especially traffic that would originate on the west side of Tennessee Pass. Tennessee Pass is not shown here, but it is between Leadville and Minturn.

[fol. 827] Now certainly any traffic that originated west of Tennessee Pass would be handled to Dotsero and over the cutoff into Denver. I do not think any would be originated east of the pass. I think the chances are it would come into Denver by the old route.

Q. Is there any chart which would indicate the amount of traffic, either actual or comparative, that originates on the old line of the Denver at a point east of Dotsero, which is passed over the cutoff?

A. No, there would not be. That would be pretty small in amount, and we have not made any analysis of that or attempted to show it.

Q. But there is some?

A. There would be some.

Q. And that, to that extent, is what we might call Eastern Lines' traffic, that is, which is credited to the Eastern Lines, or should be credited to the Eastern Lines?

A. I do not know what you mean by that.

Q. I mean the part governed by the Denver & Rio Grande mortgage as distinguished from the Denver & Rio Grande Western mortgages, or as distinguished from the Rio Grande Western's mortgage.

A. That is true, there would be some traffic moving over the cutoff that would originate in the Denver & Rio Grande's consolidated territory, and that would not be confined to [fol. 828] traffic originated between Tennessee Pass and Dotsero. There is traffic originated between Dotsero and Rifle, which originates in Denver & Rio Grande consolidated territory, and all the traffic which originates south of Grand Junction comes from that territory and goes over the cutoff.

By Mr. Nicodemus:

Q. Mr. Wyer, in your opinion, does this chart reflect with reasonable accuracy the tonnage moving over these several lines shown thereon?

A. I do not know how you could get it any more accurate than it is reflected on here.

Q. The answer is "yes"?

A. Yes, sir.

Mr. Nicodemus: We then offer it in evidence.

Examiner Kirby: May I ask who prepared the exhibit?

The Witness: These exhibits on traffic density were prepared by the trustees' organization in Denver, at my request, for use in this case.

Mr. Nicodemus: Based upon actual records?

The Witness: Yes, sir.

There is one thing more which I should say about these figures: They would include company freight. They do not have the company freight separated by itself.

By Mr. Nicodemus:

Q. That is, nevertheless, tonnage which moves over the rails?

[fol. 829] A. That is tonnage which moves over this territory.

Mr. Hoffman: May I ask another question in relation to this chart?

The Witness: Surely.

[fol. 830] By Mr. Hoffman:

Q. Is there any traffic originating at Pueblo that is sent north to Denver and over the cut-off?

A. I would not think so. I know that there is traffic which comes over the cut-off to Denver and which we move south to Pueblo, but I would not think there would be any of the reverse character. There might be an exceptional movement, but, generally speaking, that would not occur.

Q. Would it be easily possible to ascertain that?

A. No, it would not. It would be very difficult to ascertain that.

Q. Would it be easily possible to ascertain the other information which I discussed with you before, with relation to the traffic moving west over the old Denver and Rio Grand Lines and passing over the cut-off east?

A. It would be very difficult to do it. You would have to analyze every way-bill in order to get that information.

Examiner Kirby: How large an item is the company freight in these tonnage figures?

The Witness: It is about 17 per cent of the total. Of course it varies each year but, generally speaking, it would run about that percentage of the total.

Examiner Boyden: That percentage applies to the entire [fol. 831] system?

Mr. Nicodemus: Not necessarily so.

The Witness: That is a system average figure. I am going to say a good deal about company freight later on.

Mr. Nicodemus: We will try to develop that. We renew our offer of the chart for 1935.

Examiner Kirby: Is there any objection to the receipt of this exhibit?

(No response.)

If not, the Traffic Density Chart is received as Exhibit No. 21.

(Exhibit No. 21, Witness Wyer, was received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, have you a chart for 1934?

A. Yes, I have.

Q. Have you any comments to make on that which are different from the comments you made for the chart covering the year 1935?

A. No, sir. I think the chart shows almost exactly the same, except for this one thing: That 1934 only contemplated or only included 6½ months of operation over the cut-off, and consequently, the changes in distribution of traffic due to the cut-off are much less marked on this exhibit than [fol. 832] they were on the one for 1935.

Q. Then, in 1933 the cut-off was not in operation at all. Do you have a chart for that year, also?

A. Yes, sir.

Examiner Kirby: Do you offer this in evidence?

Mr. Nicodemus: I will in a minute.

By Mr. Nicodemus:

Q. Have you any comment to make on the chart for 1933?

A. Yes, I have some comment to make on that. I would like to ask you to compare the chart for 1933 with the chart for 1935, and note particularly that in spite of the fact that the total traffic of the company was very much heavier in 1935 than it was in 1933, the traffic on the line from Dotsero to Denver via Pueblo is substantially less in 1935 than it was in 1933.

For example, take the territory from Minturn to Salida and the traffic density decreased from 990,000 net ton miles per mile of road to 770,000 or a decrease of 22 per cent.

Examiner Boyden: Eastbound?

The Witness: Eastbound, and westbound it decreased from 634,000 to 469,000.

Now taking it between Denver and Pueblo, for example, southbound, it decreased from 445,000 to 248,000, which is [fol. 833] almost half—not quite, and northbound it decreased from 794,000 to 682,000. Those represent in part

the loss by that line experienced by reason of the cut-off. They do not represent the whole loss, because the traffic level of the system had increased during those two years, but in spite of that increase, those losses still appear in the traffic handled by that line east of Dotsero, and we will submit some figures to show in dollars and cents exactly what that meant to the earnings of that particular portion of line, but this shows you physically part of what it amounts to.

Examiner Kirby: Was not the Dotsero cut-off in operation during a part of the year 1933?

The Witness: No, sir, that was opened June 15th, 1934.

Mr. Nicodemus: We offer the chart for 1933 in evidence.

Examiner Kirby: The chart for 1935 has been received as Exhibit No. 21. Is there objection to proposed Exhibit No. 21-A and 21-B?

(No response.)

Examiner Kirby: If not, the density chart for the year 1934 is received as Exhibit No. 21-A and the traffic density chart for the year 1933 is received as Exhibit No. 21-B.

[fol. 834] (Exhibits Numbers 21-A and 21-B, Witness Wyer, were received in evidence.)

Mr. Hoffman: May I ask a question Mr. Wyer?

Mr. Wyer: Yes, sir.

By Mr. Hoffman:

Q. Do these charts or will any subsequent charts about which you will testify, indicate in any way the amount of traffic originated by the Denver on its own road and destined to points on its own line?

A. There will be the converse of that, there will be the traffic interchanged by the Denver with other roads, and I will give you figures as to the total traffic handled by the Denver, so that you can get the figure which you want by subtracting the two.

Q. Also you will have figures originated by the Denver and delivered to other lines?

A. Yes, and also originated by other lines and delivered to the Denver.

Mr. Hoffman: Thank you.

Mr. Nicodemus: Mr. Examiners, we also offer a similar chart for 1932 and 1931. These will take Exhibit Numbers

21-D and C. I think there is nothing to be said about those earlier exhibits, is there, Mr. Wyer?

The Witness: No, sir, I do not think there is anything which need be said about those. They speak for them-
[fol. 835] selves.

Examiner Kirby: If there is no objection, the traffic density chart for the year 1932 is received as Exhibit No. 21-C and the traffic density chart for the year 1931 is received as Exhibit No. 21-D.

(Exhibits Numbers 21-C and 21-D, Witness Wyer, were received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, have you a statement showing the freight traffic handled by commodities over a period of years, and, if so, what period is covered by this statement?

A. Yes, I have. I have such a statement covering a period of years, 1928 to 1935 inclusive, showing the cars, tons and revenue to the Denver and Rio Grande Western on each of the important classifications of traffic.

Q. That is in two sections one for the Denver and Rio Grande Western and one for the Denver and Salt Lake?

A. Yes, I have an Exhibit covering each of the properties.

Mr. Nicodemus: We have copies of those and will tender them as Exhibits Numbers 22 and 22-A, and I will ask the witness if he has any comments to make on them.

The Witness: I think that this would be the best point to
[fol. 836] say a little bit about where the principle commodities, as shown on Exhibit No. 22 originate, and how they move, so as to give you a picture of the distribution of these commodities over the system, and if you will refer to Exhibit No. 22 in connection with Exhibit No. 21, I think that will be a convenient way of handling it.

From Exhibit No. 22 you will note that the principle revenue-producing-commodity on the Denver and Rio Grande Western is coal and coke which accounted for a revenue of $3,315,000.00 in 1935.

I have already pointed out some of the principal originating territories for this commodity, which is in and around Helper, and that movement is nearly all west to Salt Lake Valley, and to connecting lines at Salt Lake and Ogden.

The other principal originating coal fields are in Southern Colorado, in and around Walsenburg, which is directly south of Pueblo. There are fairly extensive mines in the Walsenburg territory, and also coal mines all the way south from Walsenburg through Rouse, down to Trinidad and Bon Carbo.

There are also a couple of mines just west of Walsenburg, near the place shown as Tropic, and a branch running north of Walsenburg to Alamo, which is entirely a coal-producing [fol. 837] branch. That coal goes principally north to Pueblo and Denver and points east of those junctions in Colorado, Kansas and Nebraska.

Then there are some smaller coal fields near Colorado Springs. There is one fairly large mine there. There is coal near Canon City, which is about 40 miles west of Pueblo. The branches serving Chandler and Fremont are coal branches.

There is coal on the narrow gauge, as I have already pointed out at Crested Butte. That is what we call anthracite coal. I do not think it quite compares with the Pennsylvania anthracite, but it is much the hardest coal produced anywhere in the Rocky Mountain region, and that is why it is worth while to haul this coal out over narrow gauge lines at extremely great cost, carry it over Marshall Pass and bring it east from Salida.

Mr. Hoffman: You spoke of the narrow gauge line at Crested Butte, and I would just like to ask about the line between Pueblo and down through Mustang down there, where the heavy traffic is. Is that narrow gauge or standard gauge?

The Witness: Standard gauge.

Mr. Hoffman: Standard gauge?

The Witness: That line is a joint double track, one [fol. 838] track of which is owned by the Denver and Rio Grande Western, and one which is owned by the Colorado and Southern.

Mr. Hoffman: Is that the only standard gauge?

The Witness: I have already outlined exactly where the narrow gauge lines were, and everything else is standard gauge.

Examiner Kirby: You have a map already presented showing the narrow and standard gauge?

The Witness: Yes, sir, Exhibit No. 7, I think it is, shows the narrow gauge lines exactly, and I have already covered it orally.

Another important class of traffic is refined petroleum, principally gasoline. That accounted for $880,000.00 of revenue in 1935. Most of this is received from points off line and moves to local points on the system. About half of that comes from refineries in California and moves east on to the system, or from refineries in Wyoming, the Casper Field, moving on to the system through Denver.

There are also refineries on the system which originate the other half of this traffic, located at Salt Lake City, which moves east at Denver, at Florence, which is just west of Pueblo on the main line, and at Farmington, New Mexico, [fol. 839] which is on the narrow gauge south of Durango, the very southwestern corner of the narrow gauge. The Farmington refinery serves the narrow gauge territory.

Then, of course, there are other products of mines.

Examiner Boyden: Just a minute before leaving the oil. Where does the oil from Farmington move to? Denver?

The Witness: That is gasoline. It moves principally to the local narrow gauge territory. None of it comes on to the standard gauge. It just serves that narrow gauge country.

The classification which is shown on Exhibit No. 22 as "Other Products of Mines," which includes ores and concentrates, accounted for a little over $2,000,000.00 of revenue in 1935, and that is scattered very generally over the system.

The Utah production is on the Silver City Branch and the Goshen Valley is one of the lines serving metal mines in that territory. The Park City Branch has mining activity on it. In fact, those two branches are operated almost exclusively to serve the mines.

The branch to Bingham serves a copper mining territory there.

And in Colorado around Leadville on the standard gauge, [fol. 840] between Salida and Minturn and around Silverton on the narrow gauge northeast of Durango are the principal mining sections.

There is also mining activity at a great many points in smaller amounts in Colorado and Utah.

Examiner Boyden: How does the production of mines in Utah move? Does that move to Salt Lake City?

The Witness: The production of mines in Utah almost all moves to the smelters in the Salt Lake Valley. That would be at Midvale, Garfield and Murray, in between Midvale and Salt Lake City. Midvale is just ten miles south of Salt Lake on the main line, and Garfield is directly west of Salt Lake City on the branch. There is another small smelter in between Salt Lake City there, and at Murray, which is a larger smelter.

There is usually a smelter operating in Leadville and at times there is a smelter operating at Durango. Of course, the Leadville smelter gets his ore from that territory, and Durango gets its ore from the Silverton territory.

There is a cyanide mill at Colorado City, near Colorado Springs, out on the Manitou Branch, which gets traffic from other lines than the Denver.

Then the fresh fruits and vegetables, included in the products of agriculture, originate at a good many points [fol. 841] on the system. There is a large originating territory south and east of Grand Junction, around Palisade, which is on the Rio Grande Junction Railway just east of Grand Junction, and between Delta and Somerset on the standard gauge line south and east of Grand Junction. There is also a good deal of this traffic which originates in the Salt Lake Valley, all through the valley, all the way up to Ogden and down on the Marysvale Branch, which is a long branch running south and a little west from Thistle, on the main line.

Then there is also a fairly large volume of traffic which originated in and around Canon City, between Pueblo and Salida, and in the San Luis Valley, which is around Alamosa. Most of that traffic moves east, wherever it originates. It goes to the main line and goes east. The San Luis Valley traffic comes to Alamosa and is concentrated there and moves east up to Pueblo and Denver over the standard gauge lines.

Then there is a great deal of this character of traffic which originates in California and is brought east by connecting lines, Salt Lake City and Ogden, and delivered there and moved east over the main line either to Pueblo or Denver, and the majority of that is given to connecting lines at those points. Some of it, of cou-se, is for local consumption.

[fol. 842] Then we have livestock, which is another important commodity. In 1935 it accounted for nearly one million dollars of revenue, and that originates practically everywhere on the system. The heaviest loading points are at Rifle on the east end of the Río Grande Junction Railway, and then south of Grand Junction at Delta and Montrose, and in Utah there is a very heavy natural shipping point at Heber, which is on the Heber Branch. Heber is directly south of Park City, and the branch joins the main line at Provo, which is south of Salt Lake City.

Then there is also a good deal of cattle loading on the Marysvale Branch and in the Salt Lake Valley. There is hardly anywhere on the system where you do not load cattle. That nearly all moves east to the stock yards at Denver, the stock yards at Omaha or at Kansas City, but it is almost entirely an eastbound movement.

Examiner Boyden: If it goes to Omaha, I suppose you would lose it at Pueblo. Is that correct?

The Witness: Omaha business would probably be lost at Denver. It would probably come to Denver. Kansas City business would likely come to Pueblo.

Examiner Kirby: Is there any kind of a stock yard at Grand Junction for collection purposes?

The Witness: They are just local yards for feeding and [fol. 843] that sort of thing. There is no slaughtering at Grand Junction.

Examiner Kirby: A collection yard?

The Witness: Yes.

Lumber is a fairly important commodity. That provided nearly one million dollars of revenue in 1935, and the greater part of that originates in the Pacific Northwest and comes over the main line, being handled to the Denver by connections on the west, and taken from it by connections on the east.

There is a small amount of local lumber which originates on the narrow gauge in southwestern Colorado, but that is not very important.

Then the item of potatoes furnished $425,000.00 worth of revenue in 1955. By far the largest originating territory for that is the San Luis Valley around Alamosa and on the Creede Branch west of Alamosa. That figure was very low in 1935. I will have a little more to say about that later on. If you will look back at some of the earlier

years, you will see that the potatoe revenue was higher than that, being $592,000.00 in 1934 and $592,000.00 in 1935.

Besides the San Luis Valley, there are some potatoes originating around the Grand Junction territory and in the Salt Lake Valley, but the principal movement is from [fol. 833] the San Luis Valley.

Canned goods is also important. I think that is lumped in this statement in "Other Manufactures and Miscellaneous."

Examiner Kirby: Packing House Products?

The Witness: No, it would not be under packing house products. I think under Manufactures and Miscellaneous, the last item in the Manufactures and Miscellaneous, that *that* includes the canned goods. That ordinarily accounts for one-half million dollars a year, or a little more, and the largest movement of that is from California over the main line to eastern connections, but there is a very substantial local movement from canning factories in Utah, which moves east over the main line, and there are also some factories at Delta and Grand Junction which move east from there.

Sugar traffic in 1935 earned $451,000.00 of revenue, and that originates in the Salt Lake Valley, principally, moving east from there, and also originates around Grand Junction and moves east from there. There is also some sugar handled from California.

I have tried to give you that outline of the principal commodities because it is used later in the development of our formula for allocating the earnings of the property [fol. 845] to the different mortgage districts. This analysis which I have forecast for you was the basis for a decision which we arrived at to allocate the earnings on a ton mile basis, with certain modifications which I will explain to you when we get to the formula.

If you will recall, all the principal classes of traffic which I have just described to you, the coal and other mining traffic, fresh fruits and vegetables, livestock, lumber, potatoes, canned goods and sugar, all these move over the whole of the main line or they originate at various parts over the system, so that their movement is very well diversified over the whole system. The only minor exception to that is the potatoes which originate principally in the San Luis Valley and move over from there, but all of these other commodities move on all of the different mortgage districts.

So that every mortgage gets the benefit of tonnage made up practically of all of these principal commodities, and we felt that that being the case, it was fair to do what I shall describe to you in detail later, that is, allocate the bulk of the revenues on this property to the mortgages on a ton-mile basis.

Examiner Boyden: There has been a recent development of oil traffic from California, has there not, quite a considerable development?

The Witness: I did not think it was very large, no— [fol. 846] not by this road.

Examiner Boyden: There has been quite an increase in oil production in California, has there not?

The Witness: Yes, sir.

Examiner Boyden: Do you recall when that began to take place?

The Witness: I do not know, because that would be principally in Southern California, and I did not know that this road was getting any of that. I should think it would come by other routes.

Examiner Boyden: Would it not affect your coal traffic?

The Witness: I have not heard of any effect on the coal traffic in this territory.

Examiner Boyden: You do not know when that development took place in California?

The Witness: No, I know generally that there has been an increase in oil production in California. That might affect a little the coal traffic moving west out of Helper, to the extent that it went to California points, but I have not heard of any effect on that movement. That would be the only place where I could see that it would be likely to affect this, and, as I say, I do not know of any such effect. I have not heard of it.

Mr. Hoffman: Mr. Wyer, reserving the point for the mo- [fol. 847] ment, do I correctly understand you to say that in substance the plan endeavors to allocate to securities on the basis of the revenues derived from the various parts of the system, using a ton-mile basis?

The Witness: Yes, sir.

Mr. Hoffman: Irrespective of the dollar price paid which is received for the product?

The Witness: I will explain that more in detail when I get to the formula which allocates the revenue, but I wanted to explain or give this summary of the principal

commodities and their movement, because that is of importance when we arrive at that point in explaining why we adopted the particular method which we adopted then, and it seemed proper to include that here because you have the specific exhibits which are pertinent before you right at this time.

Mr. Hoffman: I just wanted to know whether I understood you correctly. That is all.

By Mr. Nicodemus:

Q. Your explanation indicates that there is no statement necessary on the Denver and Salt Lake Railway Company, because you have no mortgage problems there, but perhaps you would like to make a statement about the Denver and Salt Lake.

A. The Denver and Salt Lake situation is pretty simple. If you look at 1935, you will see that out of a total revenue [fol. 848] of $2,074,000.00, they earned $1,284,000.00 on bituminous coal, or over 60 percent, and that originates, if you look at the same mortgage map again, Exhibit No. 21, west of Orestod on the Denver and Salt Lake, principally around a place called Hayden, which is between Orestod and Craig, and is brought east to Denver and used either at Denver or delivered to connections at Denver.

Their next largest commodity is petroleum, $239,000.00 earned on crude petroleum in 1935 and $166,000.00 on refined petroleum. That all originates, or nearly all, at Craig, there being a refinery at Craig, and oil production near that point comes east, partly to Denver but partly to Orestod, fro mwhich it is handled west over the cut-off and over the Denver and Rio Grande Western to local points on that line, and the crude is handled as far as Salt Lake City, and the gasoline being handled principally to local territory on the Denver and Rio Grande Western.

There is one effect of the cut-off which has been to increase the shipments of that gasoline very substantially, because formerly the territory east and west of Dotsero, if it received gasoline from Craig, had to receive it around through Denver. Of course, the crude to Salt Lake City [fol. 849] moved that way around through Denver. So that that has increased those shipments by reason of the cut-off. I think that that is all that is pertinent on the Denver and Salt Lake.

Mr. Hoffman: May I ask a question on that?

Referring to this item of coal, for instance, which produces $1,284,000.00 for the Denver and Salt Lake in 1935, did the same ton of coal that produced revenue for the Denver and Rio Grande in that column, where we have the $3,315,000.00 on Exhibit No. 22, produce revenue for both roads?

The Witness: No, I do not think there would be any duplication of coal tonnages between the two roads.

Mr. Hoffman: Not a duplication, but I mean, if there were a continuous movement of coal over the Denver system and the Denver and Salt Lake System, so that the rate was allocated between the Salt Lake and Denver, would the same ton of coal produce revenue for both roads?

The Witness: No, I do not think there would be any of that. The Denver and Salt Lake Coal, as I have explained, comes east from Hayden and that territory, into Denver and is used locally there or delivered to connections in Denver, moving east and north. I do not think that very much of it would move south out of Denver over the Denver and Rio Grande Western, because it would have to compete [fol. 850] with the coal coming up from Walsenburg on the Denver and Rio Grande Western's own rails, and there would be very little of the Denver and Salt Lake Coal which would be used on the Denver and Rio Grande Western south of Denver. There might be an occasional car that would go there, and there might be an occasional car which would move south from Orestod over the cut-off, but it would be practically negligible.

Mr. Hoffman: Other than coal, would the other commodities substantially contribute to the revenue of both roads?

The Witness: I have just described the situation on the crude oil, and gasoline, and that is true in that case. That is the only commodity that is very much interchanged between the two roads.

Mr. Hoffman: As to the rest, would you say that it was not particularly substantial?

The Witness: Yes.

Mr. Nasmyth: Mr. Wyer, these statistics which we have been discussing have been used as a basis, I understand, for arriving at your valuation of the proposed securities, as compared with the present securities? Is that right?

The Witness: These are part of what has been used. [fol. 851] You have not seen it all yet, but they will gradually unfold.

Mr. Nasmyth: But is this a fair comparison of what is likely to be in the future over the same period of years?

The Witness: I think you had better wait until you get it all before you ask that question. I will be very glad to answer it later.

Mr. Hoffman: To pursue my question one step further, would not the last answer which you gave to me indicate that the interchanged traffic between the cut-off and the Western Division was very nominal, and to that extent the cut-off contributed little to the Western Division? In other words, if there is no interchange of traffic, why the same kind of traffic contributed earnings both to the D. & R. G. W. and to the Denver and Salt Lake, would not that minimize the importance of the cut-off?

The Witness: No, because you are talking about one of the very minor reasons for constructing the cut-off.

Mr. Hoffman: I am just trying to get some information.

The Witness: The cut-off was constructed primarily to shorten the distance between Denver and Salt Lake for the Denver and Rio Grande Western. By shortening that distance 173 miles, it put the Denver and Rio Grande Western [fol. 852] in a position to compete much more effectively for transcontinental traffic. That was the primary purpose of the construction of the cut-off. There were a number of incidental advantages which arose out of that, one of which was that it increased the interchange of crude oil and gasoline between the Denver and Rio Grande Western and the Denver and Salt Lake at Orestod, and additional traffic arose out of that.

It also gave very much better service to the so-called western slope of Colorado, the territory around Grand Junction and all of the local territory west of Dotsero got very much quicker service into Denver and from there on east. But the primary reason, without which the cut-off would not have been built, was the enabling of the Denver and Rio Grande Western to handle competitive transcontinental traffic, and that is so much more important than is the interchange between the Denver and the Salt Lake and the Denver and Rio Grande Western of crude oil and gasoline, that you have got to value the importance of the cut-off from that and not from one of the minor factors.

Mr. Hoffman: I was not limiting myself to any particular class of traffic. I wanted to know whether, in substance, other than coal, to which you testified, anything originated on the Denver and Salt Lake Lines, the same ton of traffic [fol. 853] contributed revenues to the D. & R. G. W., and to the Denver and Salt Lake, and I understood your answer was in substance "No". Is that correct?

The Witness: My answer is in the record, and I think it will speak for itself.

Mr. Hoffman: We are trying to elicit the information. Is it a fact? Do you have any objection to answering the question?

The Witness: Will you read the question, Mr. Reporter?

(Question read.)

The Witness: Your question is improperly stated because it does not say what I had already testified to at all. I said as to crude oil and gasoline, there was a substantial interchange between the two roads and that contributed to the revenue of both roads. I said as to coal, there was not, but other than as to crude oil and gasoline, there is not a substantial interchange.

Mr. Hoffman: Am I correct in substance in assuming that the cut-off contributes little, if any, to the Denver and Rio Grande Western at the present time, at least other than the contribution which is created by the crude oil and gasoline?

The Witness: No, you are not correct in assuming that.

Mr. Hoffman: What are the facts?

[fol. 854] The Witness: I just got through telling you what the principal reason was for constructing the cut-off.

Mr. Hoffman: Frankly I do not understand your answer.

The Witness: I told you that the volume of traffic that the Denver had secured by reason of the cut-off—and I am speaking now of competitive transcontinental traffic—is so much greater than the revenue, and the revenue from it is so much greater than the revenue involved in interchange between the Denver and Rio Grande Western and Denver and Salt Lake that that is the most important factor in the construction of the cut-off.

Mr. Hoffman: Then it is correct that the same ton of traffic contributes revenue both to the Denver and Salt Lake and to the Denver and Rio Grande Western; is it not?

The Witness: No, because the traffic which the Denver and Rio Grande Western handles—I think I see your trouble—the traffic which the Denver and Rio Grande Western handles over the Denver and Salt Lake does not contribute any revenue to the Denver and Salt Lake. The Denver and Rio Grande Western gets all of that revenue. They pay the Denver and Salt Lake a rental for the use of that line, and they pay for it on a wheelage basis, but the revenue on that is collected by the Denver and Rio Grande [fol. 855] Western and it does not contribute anything to the revenue of the Denver and Salt Lake, but that increased traffic contributes very heavily to the revenue of the Denver and Rio Grande Western, and that increased traffic could not be handled without the cut-off.

Mr. Hoffman: You say they pay the Denver and Salt Lake on a wheelage basis?

The Witness: Yes, sir, for maintenance of way and transportation expense.

Mr. Hoffman: You had the agreement here before. What does that mean?

The Witness: Wheelage is usually computed by counting the car miles and the percentage of car miles handled by the Denver and Rio Grande Western as compared with the percentage handled by the Denver and Salt Lake, and the total expense in that territory for maintaining this track is divided in proportion to the car mileage.

Mr. Hoffman: Irrespective of the contents of the cars?

The Witness: Yes, sir.

Mr. Hoffman: And irrespective of normalcy of traffic?

The Witness: I do not know just what you mean by that. You count the cars and divide the expense that way, and there is a minimum in this contract below which the D. and R. G. W. contribution cannot fall, but with that quali- [fol. 856] fication it is divided exactly in accordance with the number of cars that the two roads handle.

Examiner Kirby: We will take a short recess.

(Thereupon a short recess was taken.)

Examiner Kirby: All right, gentlemen, let us proceed. Have you finished your explanation on Exhibits Numbers 22 and 22-A, Mr. Wyer?

The Witness: Yes, sir, I have.

Mr. Nicodemus: Mr. Examiner, I will now make another offer of Exhibits 22 and 22-A.

Examiner Kirby: You are now offering them in evidence?

Mr. Nicodemus: Yes, sir.

Examiner Kirby: Is there any objection to the receipt of these Exhibits Numbers 22 and 22-A?

(No response.)

Examiner Kirby: If not, the Exhibit showing freight traffic handled on the Denver and Rio Grande Western System is received as Exhibit No. 22, and the Exhibit entitled "Revenue Freight Carried Years 1928 to 1935", on the Denver and Salt Lake Railway Company, is received as Exhibit No. 22-A.

(Exhibits Numbers 22 and 22-A, Witness Wyer, were received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, have you prepared a statement showing the interchange of traffic between the Debtor and its prin-
[fol. 857] cipal connections?

A. Yes, I have.

Q. What is that shown in? In tons?

A. This first exhibit is shown in tons, yes, sir.

Q. That also is in two sections, one for the Denver and Rio Grande Western, and another for the Denver and Salt Lake?

A. Yes, sir.

Q. Have you any comments to make upon these two statements?

A. Yes, sir. The first page shows the interchange between the D. & R. G. W. and its principal connections for the years 1934 and 1935 inclusive, and the upper half of the sheet shows the tons received by the D. & R. G. W. from its connections, and the lower half shows the tons delivered by the D. & R. G. W. to its connections.

You will notice that of the tonnage received by the D. & R. G. W. that the Western Pacific, one of the two roads owning the capital stock of the company, delivered more tonnage to the D. & R. G. W. than any other company. In 1935 it delivered 502,000 tons. The next largest amount was delivered by the Southern Pacific, also a western connection. Of the Eastern connections, the Missouri Pa-
[fol. 858] cific, the other road owning 50 per cent of the

capital stock of the company, delivered more tonnage than any other eastern connection, 291,000 tons.

The next largest delivery was by the Burlington, 113,000 tons, and the next largest by the Union Pacific, 93,000 tons.

The deliveries by the Missouri Pacific were practically equal to the combined deliveries of the Burlington, Rock Island and Union Pacific put together, those being the next three largest connections on the east.

On tonnage delivered by the Denver, the largest delivery is to the Missouri Pacific, 615,000 tons in 1935, and the second largest is to the Western Pacific, 611,000 tons.

Mr. Fisher: May I ask a question about that exhibit?

The Witness: Surely.

By Mr. Fisher:

Q. While it is relatively small, you did not put on the tons received and delivered to the Denver and Salt Lake, for instance, the gasoline tonnage delivered for the year 1935?

The Witness: No, we did not.

Q. Would that be materially smaller than the smallest one of the others? I presume it would be.

A. Yes, sir, it would be. I will have some figures later [fol. 859] on as to what that is, in connection with the discussion of the effect of the cut-off in detail, but it would be pretty small compared with these figures.

Examiner Boyden: Would it be much of a job to break down the Exhibit No. 23 statement into a statement of tons interchanged at each location? You must have had that information to work it up.

The Witness: I do not think it is compiled that way. We have the Hollerith Machine Cards in the Auditor of Freight's Office, and the connecting line is punched on the cards, and when they sort the cards, it is sorted by connecting lines. I can tell you pretty nearly where the interchange is. But, for example, with the Santa Fe interchange it is practically all at Pueblo or Trinidad, mostly at Pueblo. With the Burlington, of course, it is all at Denver. With the Rock Island it is both at Denver and Colorado Springs, with the majority of it being at Denver. With the Colorado and Southern it would be either at Denver, Pueblo or Trinidad principally. It might be at

other points too. There are a number of interchange points with the Colorado and Southern. That is about the only one where I could not tell you where the preponderance of it would be. Walsenburg is also an important interchange point for the Colorado and Southern, because freight [fol. 860] comes over from Alamosa and is delivered to the Colorado and Southern at Walsenburg for Texas points.

The Missouri Pacific, of course, is all at Pueblo. The Union Pacific east is all at Denver. The Union Pacific west is principally at Ogden, going north into the northwest, but there would be some at Provo going to Southern California, at times the Provo interchange has been very heavy. The principal interchange, however, would be westbound coal which is delivered principally at Ogden. The Southern Pacific is entirely at Ogden and the Western Pacific is entirely at Salt Lake.

Examiner Boyden: You- statement applies to the tons received and tons delivered?

The Witness: Yes, sir, that is true in both directions.

Mr. Ewing: Mr. Wyer, may I ask a question? Speaking of the Rock Island traffic, do you get more at Denver or Colorado Springs?

The Witness: More at Denver.

Mr. Ewing: Substantially more?

The Witness: Yes- more now. Of course, before the construction of the cut-off, we got practically nothing at Denver, and got it all at Colorado Springs, but that is not true now.

Examiner Boyden: If we asked for that information [fol. 861] to be broken down actually, would it be much of a job?

The Witness: Yes, it would be a pretty big job. They would have to go back to the original way-bills to do it, or would have to re-sort their cards at best, and I do not think they could do it.

Mr. Nicodemus: Would it, in your opinion, be a serviceable job?

Examiner Boyden: That is a matter of opinion.

Mr. Nicodemus: Of course, if you think it is important, we can endeavor to do it.

The Witness: I can make an investigation and find out just how much work it would be.

Examiner Boyden: Please do that and let us know.

The Witness: If we find it is easily done, we can do it.

Examiner Boyden: If it is not going to be very difficult, I would like to have that information in the record.

Examiner Kirby: Is there objection to the receipt of this statement? If not, it is received as Exhibit No. 23.

(Exhibit No. 23, Witness Wyer, was received in evidence.)

By Mr. Nicodemus:

Q. Now, Mr. Wyer, turning to the Denver and Salt Lake, [fol. 862] have you any comment to make on this statement?

A. No, sir, I have not. The Denver and Salt Lake advised us that they did not keep that information separated by carriers, so that we could not show the breakdown on it.

Examiner Boyden: It would be a case there of going back and shuffling the cards, is that right?

The Witness: Yes, sir.

Mr. Nicodemus: We offer the statement pertaining to the traffic interchanges between the Denver and Salt Lake and its connections, as Exhibit No. 23-A.

Examiner Kirby: Is there objection to its receipt?

(No response.)

Examiner Kirby: If not, it is received as Exhibit No. 23-A.

(Exhibit No. 23-A, Witness Wyer, was received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, you referred a few moments ago to the overhead traffic. Are you now prepared to explain that by reference to an exhibit?

A. Yes. I prepared an exhibit showing for the year ended June 30, 1935, the details of the overhead traffic. By the overhead traffic I mean traffic which originates on some connection east of the Denver, for example, moves over the [fol. 863] Denver and is delivered to some connection on the west. It neither originates or terminates on the Denver, but the Denver is dependent for this traffic upon its relations with other lines and upon the service which it gives in competition with other transcontinental lines for this business. This is the most highly competitive traffic which the Denver handles and this shows, by points, the overhead traffic.

The reason I think that they may not have the other by points is that the overhead traffic has been compiled this way, but I am not sure that all interchange has been compiled this way because they make separate compilations of the overhead traffic and always have. But this shows the interchanges at Provo, Salt Lake City and Ogden on the west, and shows the railroads on the east to which they are delivered.

You will notice here on the traffic received from eastbound connections, again the Missouri Pacific delivered freight to the Denver which gave a revenue of $614,000.00. That was the largest amount of any eastern connection. Of that $614,000.00, $471,000.00 was earned on through traffic which went to Salt Lake City and was delivered to the Western Pacific at that point; and $101,000.00 was on traffic which went through to Ogden and was delivered to the Southern Pacific there, and $41,000.00 was on traffic which went [fol. 864] through to Provo and was delivered to the Union Pacific at that point.

In the other direction, take traffic received from the Western Pacific at Salt Lake City, and the Denver earned on that revenue of $1,618,000.00, and of that the majority of it, $849,000.00 was carried through to Pueblo and delivered to the Southern Pacific at that point.

You will notice in each case that the majority of the Missouri Pacific's interchange was delivered to the Western Pacific and in the case of the traffic received from the Western Pacific the majority of that was delivered to the Missouri Pacific on the east.

The rest of the Missouri Pacific Traffic was divided $294,000.00 to the Burlington, $226,000.00 to the Rock Island, $153,000.00 to the Santa Fe, and $70,000.00 to the Union Pacific, and $24,000.00 to the Colorado and Southern.

You can get from that the total traffic received and delivered from each important connection, and it shows you which other connection it goes to or comes from. That of course, as I say, is the most highly competitive traffic, and the traffic that can be lost the most easily by the Denver.

The total revenue earned was $5,754,000.00 in this year, and this particular year, as I have explained, was chosen because we are basing our mortgage earnings on this [fol. 865] year which was the first year after the opening of the cut-off.

Mr. Fisher: May I ask what "O. S. L." is, under Salt Lake delivered to?

The Witness: Oregon Short Line, a part of the Union Pacific, of course.

Mr. Nicodemus: I offer the statement in evidence.

Examiner Kirby: Is there object to its receipt?

(No Response.)

Examiner Kirby: If not, it is received as Exhibit No. 24.

(Exhibit No. 24, Witness Wyer, was received in evidence.)

Mr. Hoffman: May I ask a question in connection with that exhibit, Mr. Wyer?

The Witness: Surely.

By Mr. Hoffman:

Q. Do I correctly understand that you received from the Southern Pacific, according to Exhibit No. 24, $1,527,000.00 of revenue which you delivered, and set forth in that schedule?

A. Yes, sir, that is correct.

Q. And that represents 424,000 tons, as set forth on Exhibit No. 23, is that correct?

A. No, Exhibit No. 23 covers all tonnage received from the Southern Pacific. This covers only such tonnage re- [fol. 866] ceived from the Southern Pacific as was delivered to some other connection.

Q. I see. And Exhibit No. 23 includes tonnage destined to local points on the D. & R. G. W.

A. This only covers 382,000 tons. You see the figure alongside the $1,527,000.00 of revenue? The remaining 42,000 tons was evidently for local points on the line.

Q. It would require a calculation to find out in each instance what remained on the D. & R. G. W.?

A. Yes, sir.

Q. You have not got that calculation available?

A. No, I have not made that.

Q. Is my understanding correct that on the 382,000 tons delivered by the Southern Pacific it yielded $1,527,000.00? That is gross revenue, I take it?

A. Yes, sir.

Q. As compared with the $1,618,000.00 and 402,000 tons from the Western Pacific?

A. That is correct.

Q. Where is the tonnage from the Missouri Pacific?

A. That is under the right hand column in the second block next to the last line opposite Missouri Pacific Railroad, namely, $614,542.79.

Q. Representing 98,000 tons received?

A. Yes, sir.

[fol. 867] Q. Or delivered?

A. That is tonnage received from the Missouri Pacific.

Q. Sir?

A. That is tonnage received from the Missouri Pacific at Pueblo.

Q. Of which 74,000 found its way over the Western Pacific?

A. That is correct.

Examiner Kirby: Mr. Wyer, does this Exhibit relate only to the Denver and Rio Grande Western Railroad Company?

The Witness: Yes it does. Of course, the Rio Grande Junction and the Goshen Valley and the Denver and Salt Lake Western are all leased lines, so that they are included in these figures.

Examiner Kirby: But not the Denver and Salt Lake Railway?

The Witness: No, sir, that is not included.

Examiner Kirby: None of the traffic represented on this Exhibit came to rest on the Denver and Rio Grande?

The Witness: No, sir, none of it did. They got it from somebody else and gave it to somebody else.

Mr. Nicodemus: I offer the Exhibit.

Examiner Kirby: Is there objection to the receipt of this Exhibit?

[fol. 868] (No Response.)

Examiner Kirby: If not, it will be received as Exhibit No. 24.

(Exhibit No. 24, Witness Wyer, was received in evidence.)

* * * * * * * *

[fol. 869] Mr. Nicodemus: I would like to offer this summary now as an exhibit, and offer it as a summary and with the understanding that we are to follow it up by introduc-

ing the originals of the different mortgages that are summarized in this exhibit, reserving to all counsel the right to object to any legal conclusions that are set forth in the summary and which may not be supported by the mortgages, by the basic documents.

Mr. Hoffman: And with the understanding, Mr. Examiner, that this represents only the position of the Debtor, and that the failure to object to any of the testimony does not constitute an acquiescence in it.

Examiner Kirby: Well, I understand that it is being presented as the Debtor's evidence and their conclusions; is that correct?

Mr. Nicodemus: Correct.

Mr. Anderson: Subject to the reservations I have already made.

Examiner Kirby: Subject to the reservations noted. You may proceed.

Mr. Nicodemus: Well, we will introduce it and take it as exhibit 28.

Examiner Kirby: Subject to the reservations indicated by the various parties, the document relating to description of obligations is received as exhibit No. 28.

(Exhibit 28, Witness Wyer, received in evidence)

[fol. 870] The Witness: I will arrange to do that.

The next document which I would like to present is the First Trust Mortgage of the Rio Grande Western Railway Company to The Central Trust Company of New York, dated July 1, 1889.

Examiner Kirby: Do you offer that in evidence?

Mr. Nicodemus: We offer that in evidence.

Examiner Kirby: Is these objection to the receipt of the document just tendered?

(No response.)

If not, it is received as Exhibit No. 32.

(Exhibit 32, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Now, Mr. Wyer, before you comment on that, if you wish to comment on it, have you any supplements to that mortgage?

A. Yes, sir.

Q. If so, how many?

A. There are five supplemental indentures which have been made in connection with that mortgage.

Q. Will you mention the dates of those supplemental indentures?

A. They are dated as follows, and as I give each date I will give a very brief summary of what the supplemental indenture covers, because we do not have copies for gen-
[fol. 871] eral distribution.

March 24, 1899, covered lands acquired in connection with the change of track from narrow gauge to standard gauge, and also covered 61.63 miles of constructed standard gauge railroad and telegraph line from Thistle to Manti, Utah, which is the north end of the Marysvale branch.

January 28, 1902,——

Mr. Nicodemus: One minute.

We offer the supplemental indenture of March 24, 1899, as exhibit 32-A.

Examiner Kirby: If there is no objection, it is so received.

(No response.)

(Exhibit 32-A, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Go forward to the next one.

A. In connection with that, these supplemental indentures are bound together, perhaps you could offer them as one exhibit.

Examiner Kirby: They are bound in one document?

Mr. Nicodemus: Yes.

Examiner Kirby: I withdraw the ruling.

(Admission of exhibit 32-A, Witness Wyer, temporarily withheld.)

The Witness: The second supplemental indenture is dated
[fol. 872] January 28, 1902, and covered certain land in Carbon County, Utah.

The third supplement is dated December 20, 1924, and covered the assumption by the Denver & Rio Grande West-

ern Railway Company of the mortgage bonds outstanding under this mortgage in the hands of the public.

April 1, 1925, was the date of the fourth supplemental indenture and this covered an assumption by the Denver & Rio Grande Western Railroad Company of the obligations under the mortgage.

The description of that supplemental indenture on the summary page of this exhibit which I am going to present is slightly inaccurate. It describes it as "Assumption of mortgage bonds held in Treasury."

The important part of that supplemental indenture was the assumption of the obligations under the mortgage; it was done in order to make the mortgage bonds held in the Treasury an obligation of the railroad company.

Mr. Anderson: I suppose our reservation would apply to the expression of the legal opinion of the effect or purpose of the document?

Examiner Kirby: It does, yes; but if you wish in case you see a particular instance where you wish to note an objection, you may do so.

Mr. Anderson: I know from experience that Mr. Wyer is [fol. 873] a very accurate witness, but I do think that there are some very nice questions of law involved in this case as to these liens, and I would object to that statement specifically.

Examiner Kirby: Well, a general reservation has been made in regard to that character of testimony.

Mr. Anderson: But I move that that particular statement as to the effect or purpose of that supplemental indenture be stricken, because it must be a conclusion, and I am sure that Mr. Wyer will limit his testimony accordingly so that I do not have to make these objections.

I move that that statement be stricken out now because I do not think it is appropriate in the record.

Examiner Kirby: Of course, the statement will speak for itself.

Mr. Anderson: And I think his statement of the legal effect is not admissible and I do not think it ought to be put in the record, because it is misleading, and I do not think Mr. Wyer intends to do that.

The Witness: I am perfectly willing to modify my statement to say simply that the description of the fourth supplemental indenture as shown on the summary sheet should

be changed to say, instead of "Assumption of mortgage bonds held in Treasury," it should say, "Covering assumption of obligations under the mortgage."

[fol. 874] Examiner Kirby: Who prepared the description in question?

A. It was prepared in my office, under my supervision.

Q. It is not a part of the document itself?

A. No, sir; this is simply a summary sheet describing these different supplemental indentures by date and a very brief summary of what they contain.

Mr. Nicodemus: This is the March 29, 1932, supplement?

A. No, sir; this is the April 1, 1925 supplement.

This same wording that I am now discussing appears on all the summary sheets of these supplemental indentures, and I want simply to change the wording in the description to agree with what I believe to be a more accurate description of the supplemental indenture itself.

Examiner Kirby: Then do I understand you to mean that you are now correcting your statement which you yourself had prepared?

A. Yes.

Examiner Kirby: With the reservation indicated by Mr. Anderson, the corrected statement as made by the witness may stand.

The Witness: The fifth supplemental——

Examiner Boyden: The request that the previous statement be stricken is granted.

Mr. Anderson: Now, off the record.

[fol. 875] (Discussion off the record.)

Examiner Boyden: The corrected statement is accepted, with the reservations, and the previous statement is stricken.

The Witness: The fifth supplemental indenture is dated March 29, 1932, and covered granting of authority to the Denver & Rio Grande Western Railway Company to sell or pledge the mortgage bonds issued under this mortgage and held in the Treasury at that time.

They aggregated $10,000 in amount.

By Mr. Nicodemus:

Q. Now, you also have a summary sheet, have you not?

A. The summary sheet is what I have been reading from,

and that has been distributed. The supplemental indentures themselves are attached to the summary sheet.

Mr. Nicodemus: Now, Mr. Examiner, in spite of the fact that these supplemental indentures are bound together, we would like to have them given separate exhibit numbers, so we offer the supplemental indenture of March 24, 1889 as exhibit 32-A; the supplemental indenture of January 28, 1902 as exhibit 32-B; the supplemental indenture of December 20, 1924 as exhibit 32-D, and the supplemental indenture of March 29, 1932, as exhibit 32-E; and we ask that the summary sheet be designated as exhibit 32-F.

And we offer each of those documents as a separate ex-
[fol. 876] hibit.

Examiner Kirby: Subject to the reservation already noted, the exhibits are received as offered.

(Exhibits 32-A, 32-B, 32-C, 32-E, and 32-F, Witness Wyer, were received in evidence.)

Mr. Hoffman: May I ask, off the record for a moment?

(Discussion off the record.)

By Mr. Nicodemus:

Q. Now, Mr. Wyer, the documents just received in evidence, exhibits 32 and 32-A to 32-F, inclusive, represent the security or relate to the security for the bonds designated in the Plan as "R. G. W. First Trusts (4 per cent)"?

A. Yes.

Q. Aggregating $15,190,000?

A. Yes.

Q. The second security in the table set forth in Section 4 of the Plan?

A. Yes.

In addition to the bonds shown in the table, there are $10,000 of these bonds which have been pledged with the Reconstruction Finance Corporation. They were the treasury bonds in connection with which the fifth supplemental indenture was made.

These bonds mature July 1, 1939. The interest rate is 4 per cent. They are a first lien on the main line of the
[fol. 877] D. & R. G. W., from Crevasse, which I pointed out on exhibit 7, the map, yesterday, as being near the Utah-Colorado state line, westward and northward to Ogden, the end of the line.

They are also a first lien on about a hundred miles of branch lines in Utah, and they are a first lien on a small amount of equipment.

Now, we shall have some exhibits later which deal with the equipment lien situation, and we have not attempted to describe that in detail in exhibit 28, because that is a very complicated question, and I shall just point out as I discuss these different mortgages, whether or not, generally speaking, they do have a lien on equipment.

By Mr. Nicodemus:

Q. Is that all you have to say with respect to those exhibits?

A. Yes.

Q. Will you pass to the next one which will be the Denver & Rio Grande Railroad Company first consolidated mortgage?

A. Yes.

I have here the original mortgage, designated, "Consolidated mortgage, the Denver & Rio Grande Railroad Company to United States Trust Company of New York, Trustee, dated July 15, 1886."

Q. That is not in sufficient numbers for distribution?

[fol. 878] A. No.

Examiner Kirby: Do you offer this as an exhibit?

Mr. Nicodemus: We offer that in evidence.

Examiner Kirby: Is there any objection?

(No response.)

The consolidated mortgage of July 15, 1886, is received as exhibit 33.

(Exhibit 33, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Now, Mr. Wyer, do you have the same situation there as you had in the previous case, are there a number of supplements?

A. Yes, there are.

Q. If so, will you describe them, briefly?

A. I have them all bound together, in one document. I will describe them by date and description.

Mr. Nicodemus: And we would like to reserve a separate number for each of those, as we did in the previous case.

Examiner Kirby: That will be satisfactory.

The Witness: The first one, dated March 27, 1890, covered certain land at Pueblo, Colorado.

The next three all cover land in Arapahoe County, Colorado. They were dated April 14, 1890, January 26th, 1891, and May 20, 1891.

There is also a fourth supplemental indenture covering land in Arapahoe County, dated September 11, 1891.

[fol. 879] The next supplemental indenture was dated January 30, 1894, and covered land in Garfield County, Colorado.

The next supplemental indenture, dated June 9, 1916, covered land in El Paso County, Colorado.

On December 20th, 1924, a supplemental indenture was executed by the Denver & Rio Grande Western Railroad Company assuming the mortgage bonds in the hands of the public.

On April 1, 1925, the supplemental indenture covering the assumption of the obligations under the mortgage by the Denver & Rio Grande Western Railroad Company was executed.

Examiner Boyden: What was the date of that one—off the record.

(Discussion off the record.)

The Witness: And March 29, 1932, there was a supplemental indenture granting to Debtor company authority to sell or pledge the mortgage bonds held in the treasury.

Mr. Nicodemus: We offer those severally and I will give you an exhibit number.

Examiner Boyden: Off the record now.

(Discussion off the record.)

Examiner Kirby: Will you proceed to designate the individual exhibit numbers of the various supplemental indentures?

[fol. 880] Mr. Nicodemus: March 27, 1890, in exhibit 33-A; April 14, 1890 is exhibit 33-B; January 26, 1891 is exhibit 33-C; May 20, 1891 is exhibit 33-D; September 11, 1891, is exhibit 33-E; January 30, 1894 is exhibit 33-F; June 9, 1916, is exhibit 33-G; December 20, 1924, is exhibit 33-H; April

1, 1925, is exhibit 33-I; March 29, 1932 is exhibit 33-J. That is all.

Examiner Kirby: And the summary has been indicated as 33-K?

Mr. Nicodemus: 33-K.

Examiner Kirby: Is there any objection to the receipt of these supplemental indentures?

Mr. Hoffman: May I just ask a question, Mr. Examiner? On the summary sheet, 33-K, is that 33?

Examiner Kirby: Right.

Mr. Hoffman: Is indicated for exhibit 33-I as purporting to be an assumption of mortgage bonds held in the Treasury, whereas the witness testified it purported to be an assumption of the obligations of the mortgage, and I would like to have it made plain at this time just what the witness really intends to say that he thinks it is.

[fol. 881] Examiner Kirby: Will you please clarify that?

The Witness: The description on the exhibit, 33-K, should be as I gave it in my testimony. The same correction should be made on all these summary sheets as I first outlined in connection with the R. G. W. first trust mortgage.

The summary sheet describes the indentures dated April 1, 1925 as assumption of mortgage bonds held in treasury, and all of them should, I believe, describe those indentures as "Assumption of obligations under the mortgage."

Examiner Kirby: The supplements are received as exhibits 33-A to 33-K, inclusive, including the summary sheet.

(Exhibits 33-A to 33-K, inclusive, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, have you any comments to make on those exhibits?

A. Those describe the security for the bonds which are described in Section 4, page 5, of the Plan as the D. & R. G. consols.

Those are the fourth and fifth items in the table of Present Capitalization.

There are $34,125,000 of the 4 per cent consols in the hands of the public, and $6,382,000 of bonds with a rate

[fol. 882] of 4½ per cent. All of the bonds are equally secured.

In addition to those in the hands of the public, there are $783,000 of these bonds pledged with the Reconstruction Finance Corporation and $662,000 of them pledged with the Railroad Credit Corporation, making a total in the hands of the public and pledged of $41,952,000.

These bonds are secured by first lien on the main line of the Denver & Rio Grande Western, starting at Denver, running south to Pueblo, west to Salida, north over Tennessee Pass to Dotsero and west to Rifle, Colorado, where the line connects with the Rio Grande Junction Railway.

Then at the west end of the Rio Grande Junction Railway, they are also a lien on about 18 miles of the line between Grand Junction and Crevasse, Colorado, where they connect with the line which is subject to the Rio Grande Western First Trust Lien.

Examiner Kirby: Mr. Wyer, all of these liens have been portrayed on a map exhibit?

A. Yes.

Examiner Kirby: Previously presented, are they?

A. Yes, they are all portrayed on the map.

Then this mortgage is also a first lien on the standard [fol. 883] gauge line south from Pueblo to Trinidad, and from Walsenburg on that line over LaVeta Pass to Alamosa, and up the Creede Branch to within a few miles of the end of that branch.

And they are also a first lien on practically all of the narrow gauge mileage.

The total mileage involved is 875 miles of standard gauge line and 683 miles of narrow gauge line.

They are also a first lien on a substantial amount of equipment, as will be set forth in a later exhibit.

Mr. Anderson: May I ask a question, off the record?

Examiner Kirby: Let's get this on the record.

Mr. Anderson: Have there been any substantial releases of property under any of the mortgages that you are now putting in?

A. No, no substantial releases.

Mr. Anderson: Would it be very much trouble to have a supplementing of the record with the releases that have

been executed under these mortgages so as to bring the property down to what is actually under them as distinguished from what was put under them? I think that would be much more accurate.

Mr. Nicodemus: I cannot remember a release under these underlying mortgages for many, many years.

Mr. Anderson: I would suggest that it would be better [fol. 884] and make it more accurate to file a summary as to those releases, as to what was covered.

Mr. Marsh: There have been quite a few abandonments of property authorized in connection with these properties. My recollection is that under schedule 5 I think something like six hundred thousand odd of book values are going to be wiped out in connection with the abandonment.

I presume that is part of the same exhibit. If there is going to be a summary of releases, it might be well to have a summary of abandonments.

Examiner Kirby: Do you contemplate presenting a statement of that character, relating to the abandonments?

The Witness: No, sir, I had not. I think I can explain what the situation is. Most of the releases under the mortgages would consist of small amounts of land which were being sold.

You would have some releases of lines of railroad; for example, the old Blue River Branch of the Denver & Rio Grande was originally under one of these mortgages, and it was abandoned and then released.

There have been other abandonments of line. To the extent that there have been abandonments of line, those lines have been eliminated from the mortgage map so that the mortgage map reflects accurately the lines of railroad [fol. 885] that are now subject to the lien of these different mortgages.

To the extent that the releases and abandonments have been of lands or facilities they are very minor. If you were to make a complete statement of all releases and abandonments, you would have a very voluminous document, more voluminous than the Form A which we discussed yesterday.

I do not think it would add anything to the case.

Examiner Kirby: Do the gentlemen press the request for that information?

Mr. Anderson: No, on that explanation; reserving the right, if we come across any reason why we should ask for

it, we may do so, but for the present the matter will not be pressed because I do not want to encumber this record with a mass of detail that has no particular place in the record.

All I want to get is a clear explanation of anything affecting the value of these securities.

Examiner Kirby: You reserve that?

Mr. Anderson: I reserve that for future discussion if I come across anything that ought to go into the record.

Examiner Kirby: Now, with respect to abandonments.

Mr. Marsh: That was tied up with the other. I think the book value of the abandonments would be considerably [fol. 886] more extensive than that of the releases. The present map eliminates property abandonments.

The Witness: Yes, it eliminates all the mileage abandoned.

Mr. Marsh: It eliminates all property abandoned, all mileage. Would that include possible abandonments since the proceeding started?

The Witness: Yes, it does.

For example, the Pagosa Springs Branch has been abandoned just recently and then has been eliminated from the map, and the figures of the Pagosa Springs Branch have been eliminated from the earning figures.

Examiner Kirby: Well, let us proceed.

By Mr. Nicodemus:

Q. Now, Mr. Wyer, have you finished with that mortgage?

A. Yes.

Q. Will you go from that westwardly to the old Rio Grande Western line?

A. The next mortgage is the Rio Grande Western Railway Company first consolidated mortgage, dated April 1, 1899.

Mr. Nicodemus: We are not submitting copies of that mortgage because it has been reproduced in full in the court record, at what page does it appear in the court record?

A. Page 806. There are, however, a number of supple- [fol. 887] ments to that mortgage which we have copies of here.

Mr. Nicodemus: Before you take up the supplements, let's get the mortgage in evidence.

We offer that by reference to the transcript of record, page 106, and ask that it be designated as exhibit 34.

Examiner Kirby: Is there objection to its receipt?

(No response.)

Examiner Boyden: Under the rules of the Commission, and in order to facilitate certification of the record to the court, I believe you should furnish a copy of it.

Examiner Kirby: Are you submitting a copy now for the record?

The Witness: No, we are not.

Mr. Nicodemus: It is already in the printed record, both of the court and of the Commission.

The Witness: We have assumed that they would be part of the evidence in this case.

Examiner Boyden: Through the stipulation at the beginning of the proceeding?

The Witness: Yes.

Examiner Boyden: All right.

Mr. Nicodemus: There seem to have been a flood of supplemental indentures to this mortgage, Mr. Wyer.

Examiner Boyden: Let me ask one question more:

[fol. 888] Q. Will you be able to furnish copies of those later on if you are requested to do so?

Mr. Nicodemus: We could, yes.

Examiner Kirby: You have offered the mortgage as exhibit 34, by reference to the court record.

Mr. Nicodemus: By reference to the record.

Examiner Kirby: As offered, it will be assigned exhibit number 34.

(Exhibit 34, Witness Wyer, was received in evidence, by reference.)

The Witness: The supplemental indentures to this mortgage, and their description, are as follows:

June 1, 1899; the supplement dated June 1, 1899 covered a change in the form of registered bonds issued under this mortgage.

That will be No. 34-A.

The supplement dated October 10, 1899, covered lands in Weber County, Utah, purchased from the Rio Grande Western Construction Company. That will be 34-B.

The second document dated October 10, 1899, submitted here, includes a deed to the same lands. That will be 34-C.

There was a third supplemental indenture dated October 10, 1899, covering specific pledge of $382,523.34 of equipment purchased from the Rio Grande Western Construc-
[fol. 889] tion Company. That will be 34-D.

The next supplement was dated January 19, 1900, and covered 11 miles of railroad in Utah County, Utah, purchased from the Rio Grande Western Construction Company; 34-E.

Mr. Anderson: Is any of that pledged under the mortgage still in existence?

A. Very little of it; it would be a small amount of it, but not much.

Mr. Anderson: Just a nominal amount of it?

A. Yes.

Mr. Anderson: That is all.

The Witness: The next supplement, dated January 29, 1900, covered 23.24 miles of railroad in Carbon and Emery Counties, Utah, purchased from the Carbon County Railway Company.

That constituted the Sunny Side Branch. 34-F.

The next supplement is dated January 30, 1900, and covered 15.00 miles of railroad in Utah and Wasatch Counties, Utah, purchased from the Utah Eastern Railway Company; 34-G.

The next supplement is dated March 19, 1901, and covered 3.25 miles of railroad in Salt Lake County, Utah, purchased from The Rio Grande Western Construction Company; 34-H.

[fol. 890] The next supplement was dated April 13, 1901, covered 2.42 miles of railroad in Utah County, Utah, purchased from The Rio Grande Western Railroad Construction Company; 34-I.

The next supplement is dated May 23, 1901, covers the pledge under this mortgage of the capital stock of the Utah Fuel Company. That carries with it a provision that the stock may be released from the pledge by payment of $6,000,000.

Mr. Hoffman: How much?

The Witness: $6,000,000.

There are six supplements dated July 20, 1908. They cover, respectively, the property of the Tintic Range Railway Company, 34-K; the Utah Central Railroad Company, 34-L; the Copper Belt Railroad Company, 34-M; the San Pete Valley Railway Company, 34-N; the Castle Valley Railway Company, 34-O; the Sevier Railway Company, 34-P. Those six supplements cover various branch lines in Utah which are, some of them, rather important in mileage.

They are all shown on the map to the extent that they are still in existence.

The next two supplements were dated January 21, 1910; and the first one covered the property of the Utah Eastern Railway Company, 34-Q; and the second one part of the property of the Carbon County Railway Company, 34-R; [fol. 891] The next supplement was dated February 13, 1929, covering certain lands in Salt Lake City, 34-S.

Now, there are three more supplements that are reproduced in the court records. The first of those was dated December 20, 1924, reproduced at page 895, covering the assumption of mortgage bonds in the hands of the public. That, I presume, will be 34-T.

Mr. Nicodemus: Correct.

The Witness: The next supplement, dated April 1, 1925, reproduced at page 897, covers the assumption of obligations under the morfgage; 34-U.

The next supplement, dated March 29, 1932, at page 903, grants the Debtor company authority to sell or pledge mortgage bonds held in the Treasury; 34-V.

Now, those last three supplements, which are, of course, important supplements and are reproduced in the court records, are typical of the corresponding supplements to all these mortgages that I have just described, as of the same dates, and being in the court record they will be available to everyone there.

In fact, they are described in the court record as being "typical" of the supplements to the other mortgages of the same dates.

By Mr. Nicodemus:

Q. And you have the usual summary which you des- [fol. 892] ignate as 34-W?

A. Yes.

Mr. Nicodemus: We offer all of those documents in evidence, severally.

Examiner Kirby: Is there objection to their receipt?

(No response.)

The documents generally described as supplements to the Rio Grande Western Consolidated Mortgage are received as offered and designated Nos. 34-A to 34-W, inclusive, including the summary.

(Exhibits 34-A to 34-W, both inclusive, Witness Wyer, were received in evidence.)

* * * * * * *

[fol. 893] By Mr. Nicodemus:

Q. Mr. Wyer, a few moments ago you spoke of a pledge of stock of the Utah Fuel Company; that stock is pledged under the mortgage that you have just introduced?

[fol. 894] A. Yes.

Q. Is there an agreement relating to the voting of that stock?

A. There is. I think perhaps before I introduce that, I ought to describe the security of this mortgage. I have not done that as yet.

Q. You have not?

A. No.

Q. Well, proceed, then, and describe the mortgage; I thought you had finished with that.

A. This Rio Grande Western Railway Company First Consolidated Mortgage, dated April 1, 1899, has outstanding under it in the hands of the public, $15,080,000 of bonds. They are shown on the third line of the table of present capitalization on page 5 of the Plan.

They are 4 per cent bonds. They mature April 1, 1949.

In addition to the bonds in the hands of the public, there are $1,396,000 pledged with the Reconstruction Finance Corporation.

They are a second lien on all of the mileage on which the R. G. W. First Trust 4's are a first lien, and they are also a first lien on 283 miles of scattered and disconnected branch lines in Utah, most of which are covered by these supple-

[fol. 895] mental indentures that I have just introduced.

They are also, as I stated, a first lien on the stock of the Utah Fuel Company and on a small amount of equipment.

Now, I have here an agreement described as agreement relating to the stock of Utah Fuel Company, dated December 20, 1924, between The Western Pacific Railroad Corporation, the Denver & Rio Grande Western Railroad Company, and the Missouri Pacific Railroad Company, and James S. Alexander, as trustee.

This agreement covers the voting of the stock of the Utah Fuel Company, creates a voting trust to handle such voting and provides as to the disposition of any dividends which may be declared on the stock of that company.

Briefly, the dividends go to the Denver & Rio Grande Western as long as there are any unpaid accumulated dividends on the preferred stock of that company, after which the dividends are payable to the Missouri Pacific and Western Pacific corporation.

There has been only one dividend on the stock of the company since the agreement was executed, that was for $250,000, and it was paid to the Denver & Rio Grande Western.

Mr. Nicodemus: We offer the agreement in evidence.

Examiner Kirby: The agreement relating to the stock of [fol. 896] the Utah Fuel Company, dated December 20, 1924, is received as exhibit No. 35.

(Exhibit 35, Witness Wyer, received in evidence.)

Mr Nicodemus: Proceed with the next one.

The Witness: Now, I also have a document which I have labeled "Description of Utah Fuel Company and subsidiaries." This consists of three pages, excluding the cover, and two attached exhibits or statements.

In order to acquaint everyone with the character of the property owned by the Utah Fuel Company, I have prepared this statement which summarizes the corporate history and describes the property, and it is accompanied by a six-year income account and a balance sheet of the Utah Fuel Company.

You will note from the income account that the company has operated at a deficit in every one of the past six years, the deficit ranging from $3,000 in 1935 to $160,000 in 1932.

From the balance sheet you will note that the company has no debt; has property carried at about fifteen million

dollars on the books, and has about a quarter of a million dollars of cash.

. . . . . .

[fol. 897] Mr. Sunderland: Mr. Examiner, representing the Trustee under the Consolidated Mortgage, under which the Utah Fuel Company stock is pledged, I would ask that this summary statement covering the Utah Fuel Company be marked at this time only for identification. This stock is subject to the first lien of the mortgage and we have made some study of the Utah Fuel Company; from a hasty examination of this summary statement it strikes me that I would prefer to have this marked only for identification, [fol. 898] to enable me to examine it further in connection with the investigation that we have made. It may be that we will, at a later time, permit it to go into evidence without objection, but I would prefer to have it simply marked for identification.

Mr. Nicodemus: We would ask a compromise with counsel, and have it accepted, subject to a motion to strike if at a later date he desires to take that course.

Mr. Sunderland: But I am not certain that this right to strike out is adequate protection for what I have in mind.

Examiner Kirby: You wish an opportunity to prepare for cross examination and to cross examine fully as to this exhibit.

Mr. Sunderland: I do.

Examiner Kirby: In view of the statement made by Mr. Sunderland, the exhibit is marked for identification, as exhibit 36. Ruling on the admissibility of the exhibit is reserved.

(Exhibit 36, Witness Wyer, was marked for identification.)

. . . . . .

[fol. 899] The Witness: The next mortgage is the refunding and improvement mortgage of the Denver & Rio Grande Western Railroad Company, dated February 1, 1924.

This mortgage is reproduced in full in the court record, at page 226. I presume that it will be exhibit 37.

Mr. Nicodemus: Exhibit 37; we offer it in evidence.

Examiner Kirby: Subject to the understanding expressed by Examiner Boyden, relative to the possible necessity of the Debtor supplying copies for the Commission's record,

the refunding and improvement mortgage just described will be designated as exhibit 37 and received.

[fol. 900] (Exhibit 37, Witness Wyer, received in evidence, by reference.)

By Mr. Nicodemus:

Q. In connection with that mortgage you have certain supplements, three, I believe, and a summary of the supplemental indentures?

A. Yes. The three supplemental indentures to this mortgage are dated and described as follows:

December 20, 1924, covering assignment and agreement relating to the capital stock of the Utah Fuel Company.

This is the agreement which has been introduced as exhibit 35. That will be 37-A.

The second supplemental indenture, dated February 13, 1929, covered five tracts of land in Salt Lake City; 37-B.

Mr. Hoffman: Exhibit 37-A and exhibit 35, are the same?

The Witness: One is the agreement itself and the other is the supplemental indenture relating to it.

The third supplemental indenture, dated January 29, 1930, covers the Kenilworth branch a piece of new construction in Carbon County, Utah; 37-C.

The summary sheet which has been distributed will be 37-D.

Mr. Nicodemus: We offer them severally in evidence.

Examiner Kirby: Is there objection?

(No response.)

[fol. 901] If not, the described supplemental indentures are received as exhibits 37-A, 37-B and 37-C, and the summary sheet as 37-D.

(Exhibits 37-A, 37-B, 37-C and 37-D, Witness Wyer, were received in evidence.)

Mr. Nicodemus: Now, Mr. Wyer, will you make a statement respecting the refunding and improvement mortgage?

A. There are $14,000,000 of these bonds outstanding in the hands of the public.

They are shown on lines 6 and 7 of the statement of Present Capitalization, on page 5 of the Plan.

There are $2,000,000 6 per cent bonds, series A. Those are the bonds that are owned, half by the Western Pacific Railroad Corporation, and half by the Missouri Pacific Railroad Company.

There are $12,000,000 of the Series B 5 per cent bonds in the hands of the public.

In addition to those bonds, there are $10,481,000 of these bonds pledged, of which $4,385,000 are pledged with the RFC and $6,096,000 with the Chase National Bank, as security for short term loans.

The security behind these bonds covers 119 miles of scattered branch lines, of which 85 miles are standard gauge, and 34 miles of narrow gauge, and it is also a lien on all of the other mileage of the company, subject to the prior [fol. 902] liens that I have already described.

In addition, there are pledged under it, $906,000 principal amount of refunding bonds of the Rio Grande Junction Railway Company and all but directors' qualifying shares of the capital stock of that company.

The refunding bonds of the Rio Grande Junction are a second mortgage on that property, there being a prior first mortgage of $2,000,000, so that the refunding and improvement mortgage in effect has a lien on the property of the Rio Grande Junction Railway Company, subject to $2,000,000 of first mortgage bonds outstanding in the hands of the public, which will be described a little later.

. . . . . .

[fol. 903] Now, I would like to say also, in connection with Mr. Gammell's question, that I had not completed my discussion of the security of this mortgage at the point at which he interrupted.

And I now would like to complete it by saying that this mortgage is a lien on all of the equipment of the company, subject to the prior liens that I have described, which, in the basis which we have used in this Plan, do not apply on all of the equipment of the company.

In other words, there is in the basis that we have adopted here, a substantial amount of equipment of the company on which the refunding and improvement mortgage is a first lien.

In other words, it is a lien on all equipment, and there are certain prior liens ahead of it, but those prior liens do not attach to all of the equipment, and in fact, there is

a substantial amount to which they do not attach, and it is [fol. 904] also, we believe, a lien on all of the equipment now subject to equipment trusts, subject to the lien of those trusts, without any other prior liens ahead of it on that equipment.

There are also some securities of joint terminal companies, at Denver, Pueblo and Salt Lake City, pledged under this mortgage, and it also has a muniment of title in $8,335,000 of D. & R. G. Railroad Company improvement mortgage bonds which matured on June 1, 1928, and which were paid off at maturity with the proceeds of the refunding and improvement bonds.

I have here for the record two copies of this improvement mortgage of the Denver & Rio Grande Railroad Company, given to the United States Trust Company of New York, Trustee, and dated June 1, 1888.

Mr. Nicodemus: We offer that document in evidence and ask that it be assigned exhibit No. 38.

Examiner Kirby: Is there any objection?

(No response.)

The copy of the improvement mortgage of the Denver & Rio Grande Railroad Company, dated June 1, 1888, is received as exhibit 38.

(Exhibit 38, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Are there any supplements to that?

A. Yes, there were two supplements to that mortgage, which I have here. These were dated December 20, 1924. [fol. 905] Mr. Nicodemus: Be 38-A.

The Witness: Covering the assumption of mortgage bonds in the hands of the public; 38-A.

And April 1, 1925, covering the assumption of obligations under the mortgage, 38-B.

Q. And the summary?

A. The summary sheet would be 38-C.

Mr. Nicodemus: We offer those, severally, in evidence.

Examiner Kirby: Is there objection to their receipt?

(No response.)

The supplements described are received as exhibits Nos. 38-A and 38-B, and the summary sheet is exhibit 38-C.

(Exhibits 38-A, 38-B and 38-C, Witness Wyer, were received in evidence.)

Mr. Nicodemus: You have nothing more to say about that mortgage, Mr. Wyer?

A. No.

Q. Now, Mr. Wyer, did the Debtor issue from time to time notes to Reconstruction Finance Corporation?

A. Yes, it did.

Q. They are not shown on this table of present capitalization?

A. No, they are mentioned over on top of page 6 of the Plan.

Q. They aggregate how many millions of dollars?

[fol. 906] A. $10,691,850.

Q. Perhaps you will state in a general way the origin of those loans and perhaps will wish to separate them as between the original loans, the Dotsero Cutoff loans and the loans covering the Denver & Salt Lake stock.

A. The original series of loans aggregated $3,950,000. Those were for general corporate purposes.

Examiner Boyden: What do you mean, Mr. Wyer, by general corporate purposes?

A. I was just going to expand on that a little. They covered, principally, payments of interest on bonds of the company, the earnings at that time, 1932, being insufficient to provide funds for that interest, and they also covered certain additions and betterments that were currently necessary to the property.

The purposes, of course, were stated in the loan applications, and moneys were applied in accordance with that purpose.

The purpose of these loans was stated in the various applications at the time as being what I have described and the funds were used for those purposes.

By Mr. Nicodemus:

Q. Now, those loans aggregated how much?

A. $3,950,000.

Q. And are they represented by five notes, as I under-

[fol. 907] stand the record?

A. Yes.

Q. Give the dates of those notes.

A. I have these notes listed here as an exhibit, and in connection with giving the dates, I think the exhibit should best be numbered.

Mr. Nicodemus: Those exhibits have already been distributed to counsel?

A. Yes.

Q. The first note is dated March 29, 1932?

A. Yes.

Q. And is in the amount of?

A. $250,000.

Mr. Nicodemus: We offer that as exhibit 39.

Examiner Kirby: In the absence of objection, this note to the Reconstruction Finance Corporation, dated March 29, 1932, is received as exhibit No. 39.

(Exhibit 39, Witness Wyer, received in evidence.)

The Witness: The next note is dated June 27, 1932, in the amount of $750,000, and would be exhibit 39-A.

Examiner Kirby: In the absence of objection, it is so received, as exhibit 39-A.

(Exhibit 39-A, Witness Wyer, received in evidence.)

The Witness: The next note is dated June 29, 1932, for $1,000,000; will be numbered 39-B.

[fol. 908] Examiner Kirby: This note, dated June 29, 1932, is received as exhibit 39-B.

(Exhibit No. 39-B, Witness Wyer, received in evidence.)

The Witness: The next note is dated April 25, 1933, for $1,000,000; will be numbered 39-D.

Examiner Kirby: This note, dated April 25, 1933, is received as Exhibit No. 39-C.

(Exhibit No. 39-C, Witness Wyer, received in evidence.)

The Witness: And the last note was dated June 30, 1933, in the amount of $950,000, and would be numbered 39-D.

Examiner Kirby: The note to the Reconstruction Finance Corporation, dated June 30, 1933, is received as exhibit 39-D.

(Exhibit 39-D, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Have you any explanation to make of those.

A. No.

Examiner Boyden: Before we pass from that, Mr. Wyer, have you prepared a statement showing the exact purposes for which those loans were used?

A. I have not, but that can be very easily done and I would be very glad to do it.

Examiner Boyden: Please.

By Mr. Nicodemus:

Q. Now, the next loan from the Reconstruction Finance [fol. 909] Corporation was the Cut-off loan?

A. Yes, sir.

Q. Have you the notes covering that loan.

A. No, I have not. There were 21 notes in this series; they aggregated $3,631,000.

[fol. 910] The proceeds were used exclusively for the construction of the Dotsero Cut-off. The last note of the series, dated August 31, 1934, is reproduced at page 50 of the court proceedings, and all of the notes are similar, this is a typical note in that series.

Mr. Nicodemus: Well, we offer the typical note as exhibit 39-E, and will refrain from furnishing the other 20 unless someone feels that they ought to be placed in the record.

Examiner Kirby: The date of that note to which reference is made is August 31, 1934.

Mr. Nicodemus: Correct.

Examiner Kirby: And is found at page 50 of the court record?

Mr. Nicodemus: Correct.

Examiner Kirby: With the understanding expressed by Mr. Boyden previously, this note will be indicated as exhibit No. 34-E, and so received by reference to the court record.

(Exhibit 39-E, Witness Wyer, received in evidence, by reference.)

The Witness: This construction was opened for operation on June 15, 1934. I do not think there is anything more need be said in connection with this.

I will describe the collateral security for all of these loans [fol. 911] later on, as in the end the security for all of these

loans from RFC is pledged and secures all of the notes, and when we come to the end, I will describe the security for all of them.

By Mr. Nicodemus:

Q. Let's take up the loan that was made in connection with the acquisition of the minority stock of the Denver & Salt Lake Railway Company.

A. This aggregated, originally, $3,182,150, which was sufficient to pay for all of the minority stock at the rate of $155 a share, the Commission having approved the purchase of the stock at that price.

Some of the stock was not turned in, 460 shares to be exact, and consequently $71,300 of the loan was repaid after the expiration date of the offer, so that the net loan today is $3,110,850.

The note covering this loan was dated December 19, 1934, and appears on page 55 of the court record.

Mr. Nicodemus: We offer it as exhibit 39-F.

Examiner Boyden: You will be able to furnish copies of that?

Mr. Nicodemus: We will.

Examiner Kirby: It is received as exhibit No. 39-F.

(Exhibit 39-F, Witness Wyer, received in evidence, by reference.)

By Mr. Nicodemus:

Q. Mr. Wyer, was there a supplemental agreement with [fol. 912] the Reconstruction Finance Corporation relative to the pledging of the Denver & Salt Lake stock for the loan covering acquisition of the Denver & Salt Lake stock?

A. Yes, there was.

Q. Will you briefly describe it for the record?

A. Well, this was dated December 19, 1934, and it is reproduced on page 63 of the court record. I do not have a copy of it here.

Mr. Nicodemus: We introduce it as exhibit 39-G.

Examiner Kirby: It is received, similar to the receipt of exhibit 39-E and 39-F.

(Exhibit 39-G, Witness Wyer, received in evidence, by reference.)

By Mr. Nicodemus:

Q. Now, Mr. Wyer, did the Reconstruction Finance Corporation also take a lien on the equities in the collateral that the Debtor pledged with the Railroad Credit Corporation?

A. Yes, they did.

Q. Have you a copy of the assignment of that equity?

A. I have.

Q. Will you produce it?

A. This has been distributed. It is dated April 21, 1933, and it is an assignment to the RFC of any equity in $662,000 of the D. & R. G. First Consolidated 4 per cent bonds, [fol. 913] pledged with the Railroad Credit Corporation at that time. I have already described that mortgage.

Mr. Nicodemus: We offer that as 39-H.

Examiner Kirby: In the absence of objection, it is so received.

(Exhibit 39-H, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Now, Mr. Wyer, did Reconstruction Finance Corporation overlook the equity in the bonds pledged to the Chase National Bank?

A. No, sir, they did not, they do not seem to have.

Q. Have they taken an assignment on that?

A. Yes. That was also dated April 21, 1933; copies of it have been distributed, and it will be No. 39-I. This relates to $6,096,000 of Series B refunding and improvement 5 per cent bonds pledged with the Chase National Bank; RFC is getting second lien on those bonds.

Mr. Nicodemus: We offer that in evidence.

Examiner Kirby: In the absence of objection, it is so received.

Mr. Nicodemus: 39-I?

Examiner Kirby: 39-I.

(Exhibit 39-I, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, have you prepared a statement showing the investment in the cut-off as of December 31, 1935?

[fol. 914] A. Yes, I have.

Q. Have you any comment to make on it before I submit it to the Examiners, and, of course, that could be separated out of these other documents.

A. It is all, I think, in the record, separately in different places. No, I do not think it is, either, I think part of it is in the record in separate places, but inasmuch as the greater part of these loans from the RFC was to enable the Debtor to construct the cut-off and complete the acquisition of the stock of the Denver & Salt Lake this seemed to be an appropriate time to put in a statement showing what the total investment of the Debtor Company is in that project, and this exhibit shows that that total investment is $12,526,376, of which amount $7,838,356 represents an investment in the capital stock of the Denver & Salt Lake Railway Company; $1,042,560 and investment in income bonds of the same company and $3,631,000, the actual cost of construction of the cut-off itself.

Plus a small amount for advances to the cut-off company.

Mr. Nicodemus: We offer the statement.

Examiner Kirby: This statement of the investment in the cut-off route is received as exhibit 39-J.

(Exhibit 39-J, Witness Wyer, received in evidence.)

. . . . . .

[fol. 915] By Mr. Nicodemus:

Q. Mr. Wyer, part of the collateral under these Reconstruction Finance Corporation loans is stock of Motorways Bus Lines, owned by the Debtor.

A. Yes. Before we discuss that, I think perhaps this is the best time to summarize the entire collateral under all of the loans.

Q. That is all right. You may do so.

A. The collateral divides itself into four groups: The first constitutes bonds which are obligations of the Debtor Company.

These are $783,000 of the D. & R. G. first consolidated 4's, that is, the first lien on the Colorado line; $10,000 of the R. G. W. first trust 4's; $1,395,000 of the R. G. W. first consolidated 4's, which is a second lien on the main line in Utah; and $4,385,000 of the refunding and improvement 5's.

Then there are the securities which are connected with the Cut-off route. They have $1,266,000 of the Denver &

Salt Lake income 6's, the second mortgage on the D. & S. L.; 49,540 shares, or 99.8 per cent of the capital stock of the D. S. L., and all of the capital stock of the D. & S. L. W., [fol. 916] which is the company owning the Cut-off, there being no bonded debt of the D. & S. L. W.

So that they, in effect, have as security all of the D. & S. L. and D. & S. L. W., except for loans of $2,000,000 first mortgage bonds of the D. & S. L. and $9,734,000 of income 6's, which rank ahead or in par with the loan of the RFC.

Then they have the stock of two motor subsidiaries of the Debtor, Denver, Colorado Springs, Pueblo Motorways, Inc., $42,000 par value, which is half of the total stock of that company, and which is all of the stock which is owned by the Debtor.

They also have $130,000,000 par value of the Rio Grande Motorway, Inc., which is 50 per cent of the total issue, and all of the stock owned by the Debtor.

In the miscellaneous group, they have the entire stock of the Goshen Valley and $1,777,000 of Rio Grande Southern Railroad Company first mortgage 4 per cent bonds. The Rio Grande Southern is a narrow gauge line which is located in the southwestern part of Colorado. It connects with the narrow gauge lines of the Debtor at two points, one of them Ar[illegible]go and the other, Ridgeway, which is just south of Montrose.

The company is in receivership, has been for a number of years, and these bonds have been in default for fourteen [fol. 917] years. I would not consider that they had any particular value.

Then they have a second lien on the securities pledged with the Railroad Credit Corporation and the Chase Bank, as I have already described.

Now, the motor subsidiaries are the only companies covered by that collateral that need any further description.

By Mr. Nicpdemus:

Q. Have you a descriptive statement with respect to the Rio Grande Motorway, Inc.?

A. No, I haven't a descriptive statement of the company, but I have an income account.

Q. An income account for 1927 to 1935?

A. For nine years, yes.

Q. Have you a balance sheet?

A. Yes.

Mr. Nicodemus: We offer those as a single exhibit, 39-K.

The Witness: You are offering both the income account and the balance sheet?

Examiner Kirby: Are they on separate sheets?

The Witness: Yes.

Mr. Nicodemus: One financial statement.

The Witness: The Rio Grande Motorway operates a very substantial mileage in the western part of Colorado and in the state of Utah. Exhibit 39-K shows the net income in [fol. 918] every year of operation. In 1935 the amount earned represented approximately 5 per cent on the debtor company's investment in this subsidiary, that investment being $228,000.

This refers to 39-K, sheet 1.

Examiner Boyden: The income account is sheet 1 and the balance sheet is sheet 2?

The Witness: That is right.

The second sheet of exhibit 39-K, the balance sheet of this company, shows that the company's depreciation reserve is invested to the extent of $106,000 in United States Government bonds.

The second motor subsidiary, the Denver, Colorado Springs & Pueblo Motorway, is also represented by an income account and a balance sheet, which will be exhibit 39-L, of two pages.

Examiner Kirby: Well, just a minute. 39-K has not been received.

Mr. Nicodemus: We offer it.

Examiner Kirby: In the absence of objection, the income account statement of the Rio Grande Motorway, Inc., is received as 39-K, sheet 1, and the balance statement is received as 39-K, sheet 2.

(Exhibit 39-K, sheets 1 and 2, Witness Wyer, received in evidence.)

[fol. 919] Mr. Nicodemus: We make a similar offer of corresponding statements of the Denver, Colorado Springs, Pueblo Motorway, Inc.

Examiner Boyden: Sheet 1, again, is the income account and sheet 2 is the balance sheet?

The Witness: Yes, sir.

Examiner Kirby: The income account statement of the Denver, Colorado Springs, Pueblo Motorway, Inc., is received as exhibit 39-L, sheet 1, and the balance sheet statement of the Denver, Colorado Springs, Pueblo Motorway, Inc., is received as exhibit No. 39-L, sheet 2.

(Exhibit 39-L, sheets 1 and 2, Witness Wyer, were received in evidence.)

The Witness: This company operates on the eastern slope of the Rocky Mountains in Colorado. The Debtor has an investment of $139,000 in it, or rather, the total investment of the company is $139,000, the Debtor owning 50 per cent of the capital stock. The earnings in 1935 were $30,000, or about 22 per cent on the investment, and this company has $70,000 in U. S. Government bonds.

I think that completes the description of the RFC loans and the security for them.

. . . . . .

[fol. 920] By Mr. Nicodemus:

Q. Have you any comment to make on this note, Mr. Wyer?

A. The loan from the Railroad Credit Corporation was used entirely for the payment of interest on funded debt of the Debtor.

I was asked this morning to give the detail of the purposes of the Reconstruction Finance Corporation loans, and this loan is tied up with the Reconstruction Finance Corporation loan, so I can now give a complete statement of the purposes of both loans for the record.

I have that information.

Q. Will you do it now, if this is a convenient time?

A. This is a good time to do it.

The first loan from the Reconstruction Finance Corporation was originally $750,000, and it was used for the following purposes:

To pay the interest on the R. G. W. Consols due April 1, 1932, $301,600.

To pay the interest on the Refunding & Improvement Bonds, due April 1, 1932, $360,000.

To pay for crossties, $88,400.

[fol. 921] Total, $750,000.

Said loan was reduced from $750,000 to $250,000 by application of the proceeds of the loan from the Railroad Credit Corporation, which was, of course, applied against the money advanced to pay interest on funded debt.

Examiner Boyden: That loan is covered by the note of March 29, 1932, is that right?

The Witness: Yes, sir, that is right.

The second loan, covered by the note of June 27, 1932, for $750,000, was used for the following purposes:

To pay the interest due July 1, 1932 on the D. & R. G. First Consolidated Bonds, $826,095.

To pay the interest due the same date on the Rio Grande Western First Trust Bonds, $303,800.

There was operating cash on hand to apply towards these obligations of $379,895, leaving $750,000 required from the Reconstruction Finance Corporation.

The third loan, dated July 29, 1932, for $1,000,000, was used for the following purposes:

To pay the interest due August 1, 1932, on the General Mortgage 5's, $745,200.

To pay in part taxes in Colorado due on August 1st, $254,800.

Total, $1,000,000.

The fourth loan, dated April 25, 1933, for $1,000,000 was [fol. 922] to apply in part against Colorado taxes for the year 1932.

The fifth loan, June 30, 1933, for $950,000, was used as follows:

To pay the interest due July 1, 1933 on the D. & R. G. First Consolidated Bonds, $826,095.

To pay the interest due the same date on the R. G. W. First Trust Bonds, $303,800.

There was cash on hand on operations available for these purposes of $179,895, leaving $950,000 required from the Reconstruction Finance Corporation.

* * * * * * *

[fol. 923] Q. Have you a copy of the General Mortgage?

A. I have.

Q. Will you describe it briefly and then hand it to the Examiner?

A. This is described as General Mortgage of the Denver & Rio Grande Western Railroad Company to the Farmers

[fol. 924] Loan & Trust Company, Trustee, dated February 1, 1924.

Q. Sufficient copies are not in hand for general distribution?

A. We do not have them here, no. I think there are plenty of copies of this particular mortgage if anybody wants them, but we did not distribute this one.

Mr. Nicodemus: We offer this mortgage in evidence as Debtor's exhibit 42.

Examiner Kirby: Is there objection to its receipt?

(No response.)

If not, it is received as exhibit No. 42.

(Exhibit 42, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, have you any statement to make with respect to the general mortgage?

A. There are outstanding under this mortgage, $29,808,000 of bonds, which are shown in line 8 of the Table of Present Capitalization on page 5 of the Plan.

They are 5 per cent bonds, which mature August 1, 1955. There are no bonds pledged in addition to those already mentioned as outstanding.

They are a lien generally upon the property of the company subject to the prior liens I have already described, including the Refunding & Improvement Bonds.

In March of 1934, the Debtor Company, having found that it was unable to pay the interest on these bonds which was [fol. 925] due February 1st of that year, proposed a plan to the bondholders whereby they would accept in cash half of the interest which had been due on February 1, 1934, and present for stamping that coupon and the two following coupons, with the understanding that those three coupons, the one paid half in cash and the other two presented for stamping, would not be presented for payment until December 31, 1935.

Q. Have you a statement showing the number of dollars, in assents to that deferment plan?

A. Yes, I have.

Q. Has that been distributed, together with the plan itself?

A. That has been distributed, together with copies of the plan.

Mr. Nicodemus: We offer that as Debtor's exhibit 43.

The Witness: That has two sheets there fastened together.

Mr. Hoffman: Have you passed 42?

Mr. Nicodemus: We have.

Mr. Hoffman: There is one question I would like to ask the witness on exhibit 42.

You stated that these D. & R. G. W. bonds were junior to the securities you had already described. Did you intend by that to indicate that they were junior to the Re- [fol. 926] construction Finance Corporation notes, to the Railroad Credit Corporation notes, and the bank debt, which you had previously described?

The Witness: If I did not say so, I should have said that they were junior to the mortgage liens which I had previously described. I think that statement is correct.

Out of the total of $29,808,000 of these bonds, coupons from $23,555,600 accepted the plan and presented the coupons. That is approximately 78 per cent.

Examiner Kirby: Is there objection to the receipt of exhibit No. 43?

(No response.)

It is received in evidence.

(Exhibit 43, Witness Wyer, received in evidence.)

The Witness: At the time of the reorganization in 1924, when this mortgage was first put on the property, it was provided that the interest for five years from the date of the mortgage would be payable at the discretion of the board.

There were certain safeguards provided in the mortgage governing the payment of that interest, but it was not a fixed charge for the first five years after February 1, 1924.

None of that interest for that five year period was paid. [fol. 927] I will discuss when I come to another point in the testimony the treatment accorded that unpaid interest, but the unpaid interest on these bonds is exceptionally large because of that feature of the mortgage, and that ought to be mentioned and borne in mind when thinking of this mortgage.

Examiner Boyden: Do you mean by that the statement of unpaid interest does include the interest for the five years?

The Witness: It does include it, yes. I think that is all that needs to be said about that mortgage at this time.

. . . . . .

[fol. 928] Q. Have you a statement of the unsecured claims against the Debtor, that is, the claims that existed at the time of Trusteeship?

A. Yes, I have.

Q. Has that been distributed?

A. Yes.

Q. From what source did you secure the information stated in that statement?

A. This statement was prepared from information furnished me by the Trustees.

Q. You believe it to be reliable?

A. Yes, sir.

Mr. Nicodemus: We offer it in evidence.

Mr. Marsh: This is the entire amount of the general creditors' claims provided for in the Plan?

The Witness: This would be the maximum amount.

Mr. Marsh: Some of these would be paid, probably, before the Plan would come down?

The Witness: Yes. I want to say as to that we are advised that a great many of these things are being paid currently in cash as the liquidated amount is determined.

Mr. Marsh: Will some of these come within the six [fol. 929] months' rule?

The Witness: Yes, a good many of them would come within the six months' rule, but the amount is not determined, the amount is in dispute as yet. To the extent that they should not be paid in cash, they would, of course, be dealt with as proposed in the Plan, but this is the maximum amount, as we are advised at this time.

Mr. Gibson: There were no unpaid claims for material and supplies furnished to the Trusteeship?

The Witness: I think such as there were of those have been paid. These are the ones that have not yet been disposed of. This does not include claims which have been disposed of.

Examiner Kirby: Is there any objection to the receipt of exhibit 45?

(No response.)

A "Summary of Claims of General Creditors" is received as exhibit 45.

(Exhibit 45, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, were any of the assets of the Debtor unpledged as of November 1, 1935?

A. Yes, there were.

Q. Have you a statement of those assets?

A. I have.

Q. Will you present it, with any explanation which you [fol. 930] care to make?

A. I have prepared a statement which I have designated as "Unpledged investments at time of filing petition for trusteeship".

While this statement includes all five of the companies concerned in the Plan, there really is not any good reason for including the assets of the Denver & Salt Lake, the Rio Grande Junction, or the Goshen Valley, as they are not in the trusteeship.

Confining this discussion to the assets of the Denver & Rio Grande Western and the Denver & Salt Lake Western, I would say simply that the unpledged assets of those companies consist almost entirely of stocks or other securities on which it is very difficult to place any valuation.

Q. Terminal property, joint property?

A. There are several lots of securities representing stocks in terminal companies which are used jointly by the Rio Grande with other companies.

About the only asset which has any real value is the fourth item on page 2, designated as Receivers' Certificates of the Rio Grande Southern Railroad Company, and I have already described the location of that property.

The interest on these certificates has been paid currently [fol. 931] and I would assume that they would have a real value somewhat approaching their face amount.

The other items of security are as I have said, either stocks representing water rights owned by the company

or terminal stocks or qualifying directors' shares, or other items which probably have no realizable value and no value to anyone except the Denver & Rio Grande Western Railroad Company.

This, of course, is submitted because that has a bearing upon the payment of unsecured claims.

. . . . . .

[fol. 932] By Mr. Nicodemus:

Q. Mr. Wyer, has the Denver & Salt Lake Western Railroad Company any indebtedness outstanding?

A. Yes, it has.

Q. By what is that represented?

A. That is represented by a note dated December 19, 1934, originally in the amount of $3,182,150, reduced by indorsement to $3,110,850.

It is reproduced on page 59 of the court record.

This note is to the Reconstruction Finance Corporation and covers the same indebtedness which the Debtor Company also owes to the Reconstruction Finance Corporation, which has been described in connection with the Reconstruction Finance Corporation debt already discussed. Both the parent company and the subsidiary were required to give these notes in connection with the loan for the purchase of the remaining stock of the Denver & Salt Lake.

Q. One of the notes is collateral to the other; is not that the exact situation?

A. Yes, I believe so.

Mr. Nicodemus: We offer that note as Debtor's exhibit 53.

Examiner Kirby: It is so received.

[fol. 933] (Exhibit 53, Witness Wyer, received in evidence.)

. . . . . .

[fol. 934] Q. Have you a copy of the first mortgage of the Rio Grande Junction Railway Company?

[fol. 935] A. Yes.

Q. Will you produce it?

A. I have it here. It is described as First Mortgage, the Rio Grande Junction Railway Company to the Central Trust Company of New York, Trustee, dated December 1, 1889.

Mr. Nicodemus: We offer that as exhibit 59.

Examiner Kirby: Is there any objection to its receipt?

(No response.)

It is received as exhibit No. 59.

(Exhibit 59, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Mr. Wyer, is there a supplement to the first Mortgage of the Rio Grande Junction Railway Company?

A. There is.

Q. And it bears date of what?

A. Of December 29, 1924. This supplement covers the assumption by the Denver & Rio Grande Western Railroad Company of the mortgage bonds in the hands of the public.

Q. Have you a descriptive statement requesting that settlement?

A. Yes. That has been distributed.

Mr. Nicodemus: We offer those documents severally as exhibits 59-A and 59-B.

Examiner Kirby: The statement in the supplemental in- [fol. 936] denture are received as exhibits 59-A and 59-B.

(Exhibits 59-A and 59-B, Witness Wyer, were received in evidence.)

The Witness: There are $2,000,000 of bonds outstanding under this mortgage, which are the bonds mentioned at the bottom of page 5 of the Plan.

They mature December 1, 1939, bear interest at the rate of 5 per cent, and are, as I have stated, a first lien on the line between Rifle and Grand Junction, part of the main line operated by the Debtor Company.

By Mr. Nicodemus:

Q. Is there a further mortgage on the line of the Rio Grande Junction Railway Company?

A. Yes, there is.

Q. Will you produce it and describe it?

A. I have two copies of the refunding mortgage, the Rio Grande Junction Railway Company to the Equitable Trust Company of New York, Trustee, dated January 1, 1929.

Mr. Nicodemus: We offer that as Debtor's exhibit 60.

Examiner Kirby: Is there objection?

(No response.)

It is received as exhibit 60.

(Exhibit 60, Witness Wyer, received in evidence.)

By Mr. Nicodemus:

Q. Will you state the bonds outstanding or issued under that mortgage?

A. There have been $906,000 of bonds issued under this [fol. 937] mortgage. They are all owned by the Denver & Rio Grande Western Railroad Company and pledged under its Refunding & Improvement Mortgage.

The bonds issued mature Janu ry 31, 1979, and carry 5 per cent interest. This mortgage is a second lien on the property of the Rio Grande Junction Railway Company.

Q. Have you a specimen of the stock certificate of the Rio Grande Junction Railway Company?

A. Yes, I have.

Q. Will you produce it?

—We offer the document as Debtor's exhibit 61.

Examiner Kirby: Is there objection?

(No response.)

Exhibit 61 is received in evidence.

(Exhibit 61, Witness Wyer, received in evidence.)

The Witness: All of this stock except directors' qualifying shares is also pledged under the Refunding & Improvement Mortgage of the Denver & Rio Grande Western Railroad Company.

. . . . . .

[fol. 938] Therefore, we felt that in setting up the fixed charges we ought to set a figure which would be safely covered by an income available for interest of $3,000,000.00. We set that figure at $2,358,445.00, which would have been covered about between 1¼ and 1.3 times during the average of these three low years, and would have been covered in each of those years.

Then we thought that the property ought to have an issue of bonds whose interest was payable if earned. We wanted

[fol. 939] to make this issue a pretty good issue, so we tried to set the amount of that income issue at a figure which would have had its charges just about covered during the first year after the opening of the cut-off, or during 1935. We estimated that the new company could earn or would have earned in 1935 about three and one-half million dollars net available for interest, and therefore we tried to set the income bonds on a basis which would have had its interest charges about covered during that period.

Exhibit B of the plan shows that the income bonds which we propose to be issued here, would have had their interest charges covered if there had been $3,241,000.00 available for interest. That is somewhat less than the $3,500,000.00 figure which I have already mentioned, but there is an Additions and Betterments fund in the plan which will be explained later, which will take up that difference. But that general consideration governs the amount of Income Bonds which we proposed under the plan.

. . . . . .

[fol. 940] (Exhibit 69, Witness Wyer, received in evidence.)

. . . . . .

[fol. 941] By Mr. Nicodemus:

Q. Well, judging the future by the past, have you an exhibit showing what you have spent in previous years for similar improvements?

A. Yes, I have.

Q. Will you produce it and describe it for the record?

A. This is described at "Charges to Investment in Road and Equipment Account" and includes such charges for four of the five companies embraced in the plan and with a note to the effect that charges on the D. & R. G. W. include the Goshen Valley.

The total of these gross expenditures by individual years reached its lowest figure in 1932 in which about $389,000.00 was spent. In 1935 $894,000.00 was spent. There are probably only two years there in which the expenditure fell below three per cent of the gross and of course a number of years in which it was very much above 3 per cent of the gross. The average for the ten year period was $3,273,000,

which would be very much more than 3 per cent of the gross revenue.

Q. That does not include expenditures of the principal debtor on leased properties?

A. Yes, it does.

Q. It does?

A. Yes.

Q. Have you a separate exhibit?

[fol. 942] A. No, this includes expenditures on—I beg your pardon—this exhibit does include some expenditures on leased lines.

For example, all of the expenditures on the Rio Grande Junction represent leased line expenditures, and the expenditures on the Denver and Salt Lake Western represent principally expenditures covering the original construction during 1935, and would, of course, represent expenditures on leased lines. They do not include on this exhibit, however, expenditures for improving the property of the Moffat Tunnel Improvement District, which is part of the leased line expenditures. With that exception it includes all expenditures on leased lines, and I have a separate exhibit covering the expenditures for improvements on property of Moffat Tunnel Improvement District.

Mr. Nicodemus: We offer this statement described by the Witness as Exhibit No. 73.

Examiner Kirby: Is there any objection?

Mr. Hoffman: I would like to ask a question first, if I may.

By Mr. Hoffman:

Q. Mr. Wyer, in connection with this proposed Exhibit No. 73, I am correct, am I not, in the understanding that these represent only the improvements that were charged to capital account?

[fol. 943] A. That is correct.

Q. And that in addition to that the regular and ordinary improvements or extraordinary improvements that perhaps there were, were charged to the regular maintenance of way and structures and maintenance of equipment?

A. That is correct.

Q. Now, do you regard that 3 per cent of the revenue is a fair amount to be set out for the purpose as indicated in the plan?

A. Yes, I do.

Q. And these represent figures taken from the books, I assume?

A. These do.

Q. I did not mean that you necessarily computed them yourself, but I mean they represent figures taken from the books of the debtor?

A. They do. I think in answering your question as to whether I consider 3 per cent a fair amount; I ought to say that I consider it a fair amount to be set apart out of income for this purpose. I do not mean by that that 3 per cent will take care of all expenditures for Additions and Betterments in the future. It would not have come anywhere near to taking care of them in the past and I know that it will not in the future, but I think it is a fair amount to set aside out of income, having in mind that [fol. 944] in certain years you may not be able to finance, and that you will need a certain minimum amount from income in order to keep operating.

Q. Now, is it not true that during the period covered by this proposed Exhibit No. 73, the charges to Investment in Road and Equipment and the charges to Operating Expenses by reason of similar items were abnormally high?

A. I would say yes, that during some years of this period that would be true. It would not be true in other years.

Q. The road has engaged in what we might call a rehabilitation program during a portion of this period, is that not right?

A. Yes, during four, possibly five years of this period I think that would be true.

Q. There *was* correspondingly large charges in that period to Income and Capital?

A. Yes.

Mr. Hoffman: All right. With that explanation I have no objection to the exhibit going in.

Examiner Kirby: Exhibit No. 73 is received in evidence.

(Exhibit No. 73, Witness Wyer, was received in evidence.)

[fol. 945] J. S. PYEATT was sworn and testified as follows:

Direct examination.

By Mr. Nicodemus:

Q. Will you state your name?

A. J. S. Pyeatt.

Q. Mr. Pyeatt, you are President of the debtor, the Denver and Rio Grande Western Railroad Company, are you not?

A. The corporation.

Q. And have occupied that position for how many years?

A. Since December 20th, 1924.

Q. You came to the company at the time of the conclusion of the last reorganization?

A. I did.

Q. Will you state, in a brief way, the condition of the property as you found it, in the concluding months of 1924?

[fol. 946] A. Very briefly I would say that the condition generally was not very high at that time as to rail, ballast and bridges, the freight car equipment and the general lack of facilities for handling the amount of business that the road had at that time, I refer particularly to the terminals, most of them terminals were inadequate and rather badly constituted for handling the work; the rail was, a good deal of it, light and much of it old. Due to the character of the size used and the lack of ballast, it was expensive to maintain for the service that the road had to give at that time.

Q. Was it the policy of the reorganized company to correct those conditions and improve the property from year to year?

A. It was. Considerable had been done the previous year by the Receiver in the way of strengthening certain of the narrow gauge lines by the purchase and laying of some relay rail, the purchase of some additional equipment, the rehabilitation of the shops and extension of the shop facilities. That work was in progress and completed the first year, most of it, after reorganization.

Q. That policy continued, did it not, up to at least the beginning of the depression?

A. Yes; the new company had what it termed a five year [fol. 947] improvement plan, and beginning in 1925 that work was carried on as rapidly as it could be economically

done and as the funds were available, and during the period from January, 1925, to the end, or to the beginning of the last trusteeship, about $40,000,000.00 were spent for improvements, divisions terminals, relaying of rail, ballasting, signalling, new equipment, rehabilitation or standardization of the old equipment. All of that was done the first four years, practically all of it, of the reorganization period.

About thirty billions of the total amount expended were chargeable to Additions and Betterments, and something over nine millions of dollars, a part of the expense of doing the work, chargeable to operating expenses, went to that account.

Q. Well, as of January 1, 1930, the property, in your judgment, was in condition for safe and economical operation?

A. Yes, it was.

Q. Well, will you now proceed forward from that date? [fol. 948] A. We have prepared a budget.

Q. That budget is for the years 1937, 1938 and 1939?

A. Yes.

Q. We want to get if we can from you—I do not know that it is vitally important, but in brief—what was done toward maintaining the property during the severe depression?

A. In common with all the roads in the country rather drastic reductions were made in operating expenses. This applied to equipment and way as well as all other features of operation, and all done in the face of a reduction in traffic beginning 1930 of about 50 per cent. In other words, the use of the property was reduced to that extent. Of course, the maintenance of equipment could not be reduced nearly a corresponding amount without seriously affecting the condition and character and economical use of the equipment.

As to the freight car equipment, there was considerable deterioration because up to 1931 very little of what would be termed heavy repairs to equipment was made. Running repairs were kept up. At the beginning of the trusteeship, as I recall, we had about 6 per cent bad order freight cars on the road, which was somewhat lower than the average of the lines in that territory.

There was some under-maintenance of freight car equip- [fol. 949] ment.

Locomotives that were needed to handle the business were kept in good condition sufficient to do the job. Some others that were not needed were not repaired, and some of those locomotives would require repairs before they are used when they are needed.

Our requirements of maintenance of way were reduced considerably. In fact, about all we endeavored to do was to keep the track well surfaced, and tie renewals that were necessary made; and "necessary" in that case would mean a perfectly safe and economical operating condition.

* * * * * * *

[fol. 950] WITNESS HORACE STRINGFELLOW

By Mr. Nicodemus:

Q. Mr. Stringfellow, I want to ask you whether Exhibit No. 77 in your judgment exhausts the possibilities of economies or whether there are further possible economies.

[fol. 951] A. No, I do not think it does. This exhibit takes in largely the overhead expense which it is very apparent will be saved in the consolidation and merger. There will undoubtedly be other savings worked out through consolidation of trains and terminals, but which at this particular time I did not have the time to go into as thoroughly as will be necessary to determine in dollars and cents the amount. There are certain offsetting items in connection with the train consolidation, and it would take quite a study to get at those savings and see what the results would be.

Q. Then you think that $212,000 a year is reasonably conservative?

A. Very.

* * * * * * *

[fol. 952] Examiner Kirby: The hearing will come to order.

This is an adjourned session of the hearing in proceedings for reorganization of the Denver & Rio Grande Western Railroad Company, Finance Docket No. 11002.

At the conclusion of the initial session of the hearing held on October 20 to 23, 1936, adjournment was taken to

December 14, 1936, but pursuant to notice from the Commission the further hearing was continued, first, to January 25, 1937, and then to this date.

Are there any changes in appearances, or are there any new appearances to be noted?

ADDITIONAL APPEARANCES

Mr. Stewart: I am William A. W. Stewart, appearing for the United States Trust Company of New York as Trustee under the Consolidated Mortgage of the Denver & Rio Grande Railroad Company, Stewart & Shearer of Counsel.

Mr. Myer: Erskine R. Myer, and Rodney J. Bardwell, Jr., representing the Moffat Tunnel Improvement District, intervener. I also represent Raymond L. Sauter, Trustee of the Denver & Salt Lake Western Railroad Company.

Examiner Kirby: Petition of intervention has been filed by the Moffat Tunnel Improvement District?

Mr. Myer: Yes, sir.

Mr. Bailey: At the original hearing in this proceeding. [fol. 953] Mr. Myer: Yes, sir.

Mr. Bailey: At the original hearing in this proceeding Mr. Clyde S. Bailey, myself, and Mr. John E. Benton, appeared on behalf of the Public Service Commission of Utah, and still so appear. In addition, however, we appear for the Uintah Basin Railroad League.

Examiner Kirby: Does that complete your statement, Mr. Bailey?

Mr. Bailey: I will have a further statement to make at the proper time, Mr. Examiner. If this is such time, I will make it now.

Examiner Kirby: Will you defer that for a moment?

Mr. Anderson: Mr. Examiner, at the original hearing on page 1 the appearance is entered as follows:

> "Henry W. Anderson (Hunton, Williams, Anderson, Gay & Moore, of counsel) and George D. Gibson, (Hughes, Schurman & Dwight, of counsel), Electric Bldg., Richmond, Virginia; and Oscar R. Ewing, 100 Broadway, New York City, N. Y., appearing for Insurance Group Committee, by George S. Van Schaick, Chairman."

That is in error. It should be:

Henry W. Anderson and George D. Gibson, (of Hunton, Williams, Anderson, Gay & Moore, of counsel), Electric Building, Richmond, Virginia; and Oscar R. Ewing, (of [fol. 954] Hughes, Scharman & Dwight, of counsel) 100 Broadway, New York City, New York, appearing for Insurance Group Committee, by George S. Van Schaick, Chairman.

Mr. Fooshee: I am Malcolm Fooshee, appearing for Guaranty Trust Company of New York as successor Trustee of the Denver & Rio Grande Western Railway Company First Consolidated Mortgage, dated April 1, 1899.

Mr. Sunderland and Mr. Fitzgibbons appeared at the first hearing for that Trustee and I am appearing at this one.

Mr. Stewart: Mr. Gerald Hughes appeared for the United States Trust Company at the first hearing, and I am Mr. Stewart.

. . . . . .

[fol. 955] WITNESS J. S. PYEATT

Mr. Nicodemus: Since the last adjournment, Mr. Pyeatt, have you made a study designed to forecast the net income available for interest for the system for a normal year?

[fol. 956] A. I have.

Q. If so, will you state the nature and extent of that study?

A. I have made in association with certain other people that I will describe more in detail in my further statement, a detailed study by commodities of freight over a period of eight years, 1928 to 1935, inclusive.

I have made the best estimate I can, based upon my own knowledge of the property, of not only the gross revenues of a normal year but the operating expenses, by certain accounts, and have prepared a statement showing the gross ton miles, excluding locomotives and tenders, but including company freight, and the net ton miles revenue freight, from 1925 to 1936, inclusive, and for a normal year; showing also the gross revenue, the cost of maintenance of way and structures and of maintenance of equipment by years, total maintenance, and separately, traffic, transportation, miscellaneous, general, and transportation for investment, credit, for each year; and the total operating expenses with

the various deductions and additions according to the ICC accounting, for both the Denver & Rio Grande Western and the Denver & Salt Lake.

I beg your pardon. This does not show more than the principal items of operating expenses of each company, and [fol. 957] omits the additions and deductions, taxes, rentals, etc., below that, which will be shown in another statement.

By Mr. Nicodemus:

Q. Have you finished your description of this statement?
A. Yes.

Mr. Nicodemus: We offer the statement in evidence and ask it be designated as exhibit 117.

Examiner Kirby: It is received in evidence.

(Exhibit No. 117, Witness Pyeatt, was received in evidence.)

Mr. Gibson: If your Honor please, I would like to reserve a motion to object to this exhibit when we have had an opportunity to examine more fully the data from which the revenues for a normal year have been computed.

Examiner Kirby: You would like to reserve the right to move to strike later?

Mr. Gibson: Yes.

Examiner Kirby: That is understood.

Examiner Boyden: Before you leave that, I would like to find out what is meant by the normal year, on the exhibit.

The Witness: That is a little bit difficult to describe precisely, but it is the year when occur all of the flush or unusual traffic movements to take care of the lack of construction of [fol. 958] all sorts, and the lack of activity during the depressed period.

We have assumed, as we experienced last year and are experiencing now, that the railroads would have for a period of time an unusual increase in traffic, just as they had an unusual decrease in traffic by large percentages; that when the deferred work and business of the country is caught up through these unusual percentages of increase in activity, we will arrive at a normal condition of the country and a normal business of the country.

When that time will be depends on a lot of different conditions, but we have assumed in these statements that we would cease having an unusually large percentage of in-

crease in revenues and traffic somewhere around the latter part of 1938 and the first part of 1939.

In other words, 1939 will probably be a normal year, in our assumptions, and 1937 and 1938 will show abnormal increases.

Examiner Boyden: And in determining normalcy, have you used traffic conditions prior to the depression as a basis, or have you assumed some other level?

The Witness: We have used several levels. I would like to state the basis that we have used in trying to arrive at a proper normal year of earnings and expenses in presenting the detailed analysis by commodities, showing the [fol. 959] total cars each year for eight years ending 1935, the total number of tons of each commodity, the average carload, the total revenue, and the revenue per ton.

We have shown also the same information for nine months of 1936 compared with 1935, together with the average of the eight years of each commodity and each of these items, and below that what we believe will be a normal year, say in about 1939, of movement in each of these commodities.

Examiner Boyden: Is this another exhibit you have prepared?

The Witness: Yes. I am ready to present this now.

By Mr. Nicodemus:

Q. The next exhibit is a forecast of revenue, is it?

A. Freight revenue, together with a statement on the front of the exhibit showing not only the primary classifications of the different commodities, but the revenues by different classes of passenger traffic for eight years, the average for eight years, and the forecast for a normal year, the total revenues, freight and passenger, and the total expenses by the usual classifications, the percentage of the gross of each, and finally, at the bottom of the statement the amount available for interest, for the Denver & Rio Grande Western; and a similar statement, which can be a supplement [fol. 960] to that exhibit, perhaps, for the Denver & Salt Lake Western.

Examiner Kirby: Do you have a separate statement for the Denver & Salt Lake Western?

The Witness: Yes.

Examiner Kirby: We will let the latter statement be marked No. 119.

Mr. Nicodemus: The Denver & Salt Lake will be 119?

Examiner Kirby: The Denver & Rio Grande Western, which you first mentioned, is exhibit 118.

By Mr. Nicodemus:

Q. What assistance did you have in the preparation of these exhibits, 117, 118 and 119, can you tell that?

A. A conference was arranged at Chicago, at which we attempted to have to assist us in arriving at a proper estimate of freight traffic for a normal year, Mr. Hogan, Vice President of the Western Pacific; Mr. Perkins, Vice President of the Missouri Pacific; Mr. Taylor, Assistant Vice President of the Burlington; and Mr. Williams, the Chief Traffic Officer of the D. & R. G. W.

We were unable to get Mr. Hogan of the Western Pacific or a representative, but at the conference Mr. Taylor, assistant traffic vice president of the Burlington, who for many years previously until recently was vice president in charge of traffic of the D. & R. G. W.; Mr. J. A. Brown, As- [fol. 961] sistant Chief Traffic Officer of the Missouri Pacific; Mr. Carey, General Freight Agent of the D. & R. G. W., and myself, were present.

The statement for eight years of freight movement by commodities was before us, and we made a rather detailed study of each. The amount finally put down as the estimate of each commodity for a normal year was in every case agreed upon by Mr. Taylor, Mr. Brown, and myself. Mr. Carey dissented in most of these estimates, he having previously made, with the assistance of the traffic department of the Denver, an estimate for a normal year which was about 4 per cent above the business of last year, and which we believed did not reflect a proper estimate for a normal year.

But the three of us mentioned did agree on each item set forth in this statement, exhibit 118, of all of the commodities.

After the number of carloads was agreed upon, then the total tonnage, the average carload, and the revenue per car were figured out and stated for each item, and the total for freight arrived at of $27,884,000, and of passenger and other traffic sufficient to make a total of $30,734,000, which we present as our estimate of what a normal year will be for the Denver & Rio Grande Western.

The expenses are estimated at $22,220,682 on the basis of [fol. 962] the above revenue, with a final amount available for interest of the D. & R. G. W., of $5,198,318.

For the Denver & Salt Lake we estimate a total of $2,987,189 as a normal year's revenue, $1,697,600 as the operating expenses on the basis of handling the above traffic and properly maintaining the property, with a net amount available for interest of $1,093,065.

Q. Have you finished your description of the exhibit?

A. No, not quite. I have the description, but I would like to make some further observations on just how we did arrive at these estimates.

Q. Very good. Will you proceed with them?

A. I may say that both Mr. Brown and Mr. Taylor have expressed a willingness if necessary to support the estimates made and presented here as witnesses, if called upon.

In forecasting estimated operating revenues we first considered the volume of each commodity handled by the D. & R. G. W.—and I will say that applies also to the D. & S. L.—from January 1, 1928 to September 28, 1936, inclusive.

Second, the situation in the territory served locally by the Denver & Rio Grande Western and Denver & Salt Lake affecting each commodity at the present time and our idea of what that situation ought to be when a period of [fol. 963] normaley should be reached.

Third, the business situation in originating territory off-line governing or influencing commodities which do not originate on the Denver & Rio Grande Western, but can and will to some extent be handled by the two roads.

Fourth, the effect of the Dotsero Cutoff, which is increasing the D. & R. G. W. proportion of many lines of traffic over that handled in past years.

Where the commodity is particularly affected by the opening of the cutoff, it has been so marked in the exhibit containing the commodity detail.

Such comment does not mean that the commodity moves exclusively over the cutoff, but a substantial proportion is competitive or overhead traffic, and thus likely to be increased through availability of the cutoff.

In other words, this new line, shorter and placing the Denver in new position on through traffic, will, we think, attract a good deal of competitive and through traffic in larger proportion than we otherwise would have.

Fifth, recent trends in each commodity.

Sixth, present rate levels and prospective changes, especially with reference to emergency rate increases. As to these, many of them have been eliminated and only those retained which it is felt are most likely to be granted in [fol. 964] the general proceedings now pending before the Commission.

Mr. Nicodemus: We now offer the forecast of net income for the Denver, the parent company, and for the Salt Lake, separately, and ask that the first be designated exhibit 118 and the second exhibit 119.

Examiner Kirby: Any objection?

Mr. McKinney: The principal traffic going east which you will get because of the cutoff will be lumber, grapes, and citrus fruits, will it not?

The Witness: No; nearly every class of traffic moving from the Pacific Coast and the Northwest, canned goods, lumber, every sort of vegetables, fruits, and stuff produced in the West and imported through the West.

Mr. McKinney: During the last few months the car loadings of the road have increased sharply. Was that partially due to the fact of the longshoremen's strike on the Pacific Coast, or were most of these increases normal increases?

The Witness: No, they have not increased out of proportion the last few months. They have increased very rapidly the last fifteen months. Last year shows, I think, one of the highest increases of the Western lines on the Denver & Rio Grande Western. Car loadings have been materially heavier than in recent years.

[fol. 965] Mr. McKinney: I had specific reference to whether the loadings in the past two months had been affected peculiarly by the longshoremen's strike on the West Coast.

The Witness: No. The increased earnings the last two months are not as high as for the year 1936. The last week in January they were 18.33 per cent increase over last year, and for the period, 14.96 as against the increase of—I do not recall the per cent, but it was 24 or 25 per cent for the year 1936, but still comparing very favorably with all of the Western lines.

Mr. Fisher: May I ask you a question, Mr. Pyeatt?

In making this forecast of normal earnings, did you make a separate one for the cutoff by itself?

The Witness: No, we did not.

Mr. Fisher: Did I understand you to say that you started off on the basis of complete loss of surcharges, and then increased rates on certain commodities by what you felt was a reasonable expectation of obtaining in Ex Parte 115?

The Witness: Yes.

Mr. Fisher: Did you assume the same level of wages and wage scales as at present?

The Witness: Yes.

Examiner Boyden: As of what date does your normal year speak? It it a normal year in 1936?

[fol. 966] The Witness: No. The normal year we have in mind that we will reach and produce the figures that we have presented here for a normal year will be about 1939. That depends on quite a few factors. A good many things may occur to delay it or bring it on more quickly. But with the regular movement and increase of business of the country, we have assumed that we will reach that in about 1939.

Mr. Anderson: May I ask if you have made any allowance there for increase in commodity prices, that is, materials and supplies?

Mr. Nicodemus: In the maintenance items.

Mr. Anderson: Materials and supplies, coal, all those different commodities?

The Witness: Yes, we have assumed that those prices will be back pretty close to 1929.

Mr. Anderson: What increase over present prices have you allowed?

The Witness: We did not work out any detail on that, but we considered the prices prevailing through the period up to the end of 1929, and we based our estimate of expenses largely upon those existing during that period.

Mr. Anderson: Is not coal much higher than it was in 1929, now?

The Witness: It is a little higher. I would not say [fol. 967] a great deal higher. Other things are lower.

Mr. Anderson: Is lumber higher than it was in 1929?

The Witness: No, I do not think so. I do not have in mind the prices and I am not in touch with them, but I do not believe it is higher. I have in mind that it is perhaps lower than 1929.

Examiner Boyden: Have you provided, Mr. Pyeatt, for any increase in revenues other than those which represent

a recovery from depressed conditions, business depression?

The Witness: We allowed a very substantial increase from the so-called precious metal mining industry, which had descended to a very low level, even in 1928 and 1929, because of the price of silver, lead, and zinc. Those prices have materially improved and are considerably better than 1928 and 1929. That industry is becoming very active in that territory. There are other similar commodities where the depression after 1929 did not so materially affect them. They had already had their jolt.

Examiner Boyden: Did you assume that those commodities would go back to the pre-depression level or that they would go higher?

The Witness: Oh, much higher. Mining and scrap are higher now.

Examiner Boyden: Then you did allow for an improvement in all commodities, both in tons and in price, over the [fol. 968] pre-depression level?

The Witness: Did you say "over"?

Examiner Boyden: Over.

The Witness: No, not all. We allowed an increase in many of them because of the cutoff and the advantages of that which the road did not have prior to the depression.

Mr. Anderson: I was absent for a moment, Mr. Pyeatt. Possibly you stated, but just to get the information, what did you assume as the normal ratio of maintenance of way and structures and maintenance of equipment in the aggregate?

The Witness: 33 per cent for both of the gross of the normal year.

Mr. Anderson: You think that is a fair, normal maintenance, do you?

The Witness: I feel very sure of that.

Mr. Nicodemus: What do you figure on coal? Did you go back to the pre-depression level of coal?

The Witness: We did not figure that separately. We figured the cost of transportation based largely upon items of cost prior to 1930.

Examiner Boyden: And considering the effect of abnormal conditions in any one year, such as unseasonable weather affecting the fruit crop, and thereby affecting the traffic, you have given consideration to those factors, have [fol. 969] you not?

The Witness: Yes, we have tried to use an average production of those commodities over a period of years. We have used in every instance the average of the eight year period in arriving at our estimate of the normal year for that particular commodity, plus the Dotsero Cutoff and the recovery of traffic generally.

Mr. Anderson: I was following the work about maintenance a little further. What did you allow for maintenance of way and structures?

The Witness: 13 per cent of the gross.

Mr. Anderson: And for maintenance of equipment, 20 per cent?

The Witness: Yes.

By Mr. Nicodemus:

Q. What is your largest commodity on the Denver?

A. I would say coal. It is stated in this book.

Q. Have you estimated the increase in the coal movement over the pre-depression levels?

A. No.

Mr. Anderson: You estimated the decrease, below the average, from $4,262,630 to $3,948,750.

The Witness: The average? What is the high year?

Mr. Anderson: Six million, 1929.

The Witness: What is our estimate?

[fol. 970] Mr. Anderson: $3,948,750; but the average for the ten years is $4,262,630.

The Witness: Most of those years were very bad.

Mr. Anderson: You estimate a decrease, but in copper ore and concentrates and things of that kind you estimate an increase of over 400 per cent.

The Witness: There is no question about that, in my opinion.

Examiner Boyden: Have you any underlying data that you could present showing how you arrived at the normal year for each commodity?

The Witness: Nothing more than I have stated, and the note at the bottom of each commodity giving—well, not of each, but in most of them we have put a note which explains to some extent what we have used. But I have stated the elements that we used generally in arriving at these estimates.

Examiner Boyden: You did not state, of course, the elements that you considered in each particular commodity, but you say there in the exhibit in the form of a footnote——

The Witness: There is certain information about the average for eight years, the influence of the cutoff, the increased activity, the increased growth of the country, a comparison with 1936 business, nine months of 1936, and [fol. 971] the development of each commodity as we understand it. We tried to take into account all elements in arriving at our estimates. As I said, Mr. Taylor and Mr. Brown are with the two of the largest interchange lines with the Denver & Rio Grande Western, and Mr. Taylor was vice president in charge of traffic for many years.

They, after spending a good deal of time on each one, agreed on these estimates.

Examiner Kirby: Exhibit 119 is not in the same detail as exhibit 118.

The Witness: Not quite. We did not have the same amount of detail in that.

Examiner Kirby: You mean it was not available?

The Witness: No. I do not know that it was not available, but it was not furnished.

This is all that the Denver & Salt Lake furnished on request for the information by commodities.

By Mr. Nicodemus:

Q. Have you prepared an exhibit that combines the results of exhibits 118 and 119, to show the results for the system?

A. Yes.

Q. Will you describe that briefly?

A. This is a statement of total estimated revenues and expenses for a normal year, showing the D. & R. G. W. and the Denver & Salt Lake separately and combined.

[fol. 972] Q. The system earnings for a normal year are $33,721,189?

A. Correct. Expenses, $23,918,282.

Q. The amount available for interest?

A. $6,215,423.

Q. That estimate of operating revenues, you say, reflects your judgment, also the judgment of the traffic officials of the Burlington and the Missouri Pacific?

A. It does.

Q. And the Western Pacific?

A. The Western Pacific was not present.

Q. That is true, you say they were not. In your judgment that is a fair estimate?

A. It is.

Q. In your judgment is that estimate for operating expenses reasonably conservative?

A. It is.

Mr. Nicodemus: I now reoffer exhibits 118 and 119, and offer exhibit 120, as a group of exhibits.

Mr. Fisher: May I ask a question, sir?

In making up this statement for a normal year, did you use the Moffat Tunnel rental for the past year?

The Witness: We used the current Moffat tunnel revenue.

Mr. Fisher: It will increase?

The Witness: It will increase, but so will traffic.

Mr. Fisher: In the D. & R. G. statement by itself, before [fol. 973] being combined, that one, I take it, is assuming that the traffic agreement for the use of the joint line continues in effect as at present?

The Witness: Yes.

Examiner Kirby: Exhibit 117 has already been received.

Mr. Nicodemus: 118, 119 and 120, then.

Mr. Anderson: I think that this information may be useful, but I have not had a chance to examine it, so I would like to have it marked for identification until cross examination is completed, and then reoffered at that time. It may prove to be without foundation.

Examiner Kirby: Exhibits 118, 119 and 120 are received in evidence, subject to the general reservation of the right to move to strike after cross examination.

(Exhibits Nos. 118, 119 and 120, Witness Pyeatt, were received in evidence.)

Mr. Nicodemus: I will excuse Mr. Pyeatt temporarily.

Mr. Hoffman: May I ask Mr. Pyeatt a question in regard to a statement that he made?

Mr. Pyeatt, if I remember correctly this statement that you read, you referred to the sum of some $30,759,000 as representing additions and betterments from 1935 to 1936. Am I correct in my understanding?

The Witness: 1925.

Mr. Hoffman: 1925 to 1936?

[fol. 974] The Witness: The end of 1935, yes.

Mr. Hoffman: Did you make any similar statement for the period February 1, 1924 to February 1, 1929? That is the period during which the general mortgage was not cumulative.

The Witness: No. The statement includes the period from the time of reorganization and the new owners took charge of the Denver & Rio Grande Western, except that I believe that was December 20, 1924, and this is beginning January 1, 1925.

Mr. Hoffman: You also referred to a figure of $9,053,913, being a part of the cost of improvements charged to operating expenses that covered the same approximate ten year period, is that correct?

The Witness: Yes; 11 years.

Mr. Hoffman: Well, whatever the period is. Did you break that $9,000,000 figure down so that we might have so much of it as applied to the period from February 1, 1924 to February 1, 1929?

The Witness: No, no part of it was expended prior to January 1, 1925.

Mr. Hoffman: Would it be too much trouble to submit, just in round figures, how much of the $30,000,000 and how much of the $9,000,000 related to that five year period to which I refer?

[fol. 975] The Witness: None of it related to any period back of January 1, 1925.

Mr. Hoffman: Yes, but I do not think that I made myself clear to you, Mr. Pyeatt. From January 1, 1925, which is the period that you say this commences, until February 1, 1929, then, could we have the figure which shows how much of the $30,000,000 was expended during that period and how much of the $9,000,000 was expended during that period?

The Witness: Yes, I can separate that.

Mr. Hoffman: Would you be kind enough to?

The Witness: Give me that period again.

Mr. Hoffman: Ending February 1, 1929, and beginning whatever date these figures cover.

The Witness: February 1, 1929, from January 1, 1925.

Mr. Hoffman: Yes, sir. And would it be too much trouble also to let us know in round numbers how much of those two figures, if any, was expended after the Refunding In-

terest and the General Mortgage interest was defaulted? I think that was in 1934 some time.

Examiner Kirby: Can you do that?

The Witness: I think unquestionably we can. After the Refunding, the R. & I., defaulted?

Mr. Hoffman: After the Refunding and the General Mortgage defaulted, whichever happened to be first. I for-

[fol. 976] get offhand.

Examiner Kirby: You will supply that for the record, will you?

Mr. Nicodemus: We will supply that.

We have one more witness. I think we can finish with him very briefly, if we go ahead with him now before lunch.

Mr. Anderson: I would like to ask a question of Mr. Pyeatt.

Examiner Kirby: I assume the parties wish to defer cross examination of Mr. Pyeatt?

Mr. Anderson: I was going to ask if he could, without any serious trouble, tell me what the estimated earnings would be from now until 1939, when the normal year becomes effective, because we have to bridge that time, you know. Do you have any figures on that?

The Witness: I have not divided that up, and have made no study, no particular study, of how much of it will come during 1937 and 1938; but I believe it will all be realized in those two years; if not, a few months afterwards.

Mr. McKinney: May I ask what total traffic increase is expected in 1937 over 1936?

The Witness: I have no estimate on that.

Mr. Anderson: But you do estimate that when you reach

[fol. 977] a normal year, whenever it is, you could not even then earn your present fixed charges?

The Witness: Not quite.

Mr. Anderson: To say nothing of dividends on the preferred stock?

The Witness: That is obvious.

[fol. 978] LEONARD P. AYRES was sworn and testified as follows:

Direct examination.

By Mr. Nicodemus:

Q. Colonel, will you state your full name?

A. Leonard P. Ayres.

Q. Your occupation?

A. Banker.

Q. As a banker, have you made a specialty of any particular work?

A. Yes, of statistics, economics and finance.

Q. And normal years?

A. And normal years.

Q. How long have you pursued that particular work?

A. In that general field I have pursued that type of work all my adult years.

Q. Is it customary for your bank to issue a forecast of conditions?

A. No.

Q. Have you not a circular?

A. The bank issues, as many banks do, a monthly letter on general economic conditions, and in that connection from time to time talks about the probable future, but it does no forecasting as such.

Q. I was under the impression that your monthly fore-
[fol. 979] casts were referred to as being sometimes gloomy and ultra-conservative. Am I mistaken as to that?

A. I think, sir, you would be mistaken in assuming that there are any regular monthly forecasts from that source.

Q. But the fact is that for many years you have been engaged as an analysst in making economic studies?

A. Yes, sir.

Q. Have you in recent years directed your attention particularly to the Denver & Rio Grande Western Railway Company? I believe you came into the board.

A. I am a director of that road and have for a number of years past given special attention to its conditions and reports.

Q. Have you more recently and independently of Mr. Pyeatt made a study designed to forecast the earning power of the Denver & Rio Grande Western system in a normal year?

A. Yes, I have recently prepared such an estimate.

Q. Are you prepared to present it in the form of an exhibit?

A. I am.

Q. Would you like to make a preliminary statement respecting the exhibit, or shall I offer it?

A. If it be in order, I think that the best progress would be made by my going through the exhibit and briefly indicating what is there.

[fol. 980] Q. Our objective is progress, so we will go forward and do that.

Examiner Kirby: Suppose you produce the exhibit, and then we can identify it.

This will be identified as exhibit No. 121.

(Exhibit No. 121, Witness Ayres, was marked for identification.)

By Mr. Nicodemus:

Q. Proceed, Col. Ayres.

A. During the past ten years the operating revenues of this railroad have constituted an increasing proportion of the operating revenues of all Class I roads. There is a table on the first page and a diagram on the fourth page showing the percentage that the operating revenues of the Denver & Rio Grande Western have been during the past eleven years of the operating revenues of all Class I roads.

During that time there has been an almost steady increase, so that they were in 1926 approximately 53/100ths of 1 per cent of the revenues of all Class I roads, and in 1936 approximately 63/100ths of 1 per cent.

There was a slight depression dip in the general forward trend in 1933, but in general the road has been securing over the past decade a nearly constantly increasing proportion of the operating revenues of all the important roads.

[fol. 981] The question which I next considered was where this revenue came from, in broad terms. Did the increases come from the increases in proportion of freight carried or of passengers carried, or of other operating revenues. The results which are shown in the table on page 3 in the last three columns on the right hand side of that table give the proportions that the freight revenues of this rail-

road were of those of all Class I roads in each year, and the passenger revenues and the other revenues.

They show in brief that the increases that I have referred to have not only come predominantly from the freight, but that there have actually been in that period considerable shrinkages in the revenues from passenger and from other sources which have been a good deal more than made up by these steady increases in the freight revenue.

I then considered the question as to whether or not these increases from freight were from any special sorts of freight, or whether they were generally distributed in the different classes of freight, and the figures as to that are shown in table 3, which is on page 6.

The answer to the question is a negative one: There is no special localization of those increases.

There were in the period shown from 1928 through 1935, increases in the revenue as the proportion of the revenue [fol. 982] of all Class I roads in agriculture, animals, forests, manufacturing and miscellaneous, and less than carlot loadings, in fact, in all of the categories except those from mines, and a very minor decrease there.

So that we are clearly entitled to say that the evidence indicates that the increases in freight revenue of this road have come from well-distributed sources within the freight itself.

The question next to be considered was that of estimating the operating revenues of all Class I roads in a normal year, because if we have apparently trustworthy evidence as to the proportion of the totals that are the revenues of this road, clearly our next step must be to try to find the revenues of all Class I roads in a normal year.

I think that there is a method by which that may be done with considerable reliability, and it is in brief during the years over which our available records of such matters run, there has been a nearly constant relationship between the revenue ton miles of Class I railroads in this country, taken as a whole, and the number of factory workers engaged in what are designated as durable goods industries.

That relationship has been with considerable constancy that the roads have carried year in and year out an aver- [fol. 983] age of 100,000 revenue ton miles of freight for each factory worker engaged in the durable goods industry.

The authorities of the Federal Reserve System classify the products of industry and the workers in industry ac-

cording as they are designated as being in the durable goods industries and the non-durable goods industries.

Durable goods industries they classify as those making the things that are made from the durable materials, iron and steel, non-ferrous metals, lumber and its products, cement, stone, clay, glass, and the like, all lasting materials.

Those constitute in volume about half of all of the manufactured goods that we produce in this country. The workers engaged in making them constitute a little more than half of all the industrial workers of that sort.

In contradistinction there are the workers in the so-called non-durable goods industries, who are the people making things out of such materials as textiles, leather, paper, rubber, tobacco, gasoline, chemicals, and things of that sort.

Our records since 1919 about these industries are unusually full. The Bureau of the Census counts the workers each two years. The Bureau of Labor Statistics of the Department of Labor counts them each month. The Board of Governors of the Federal Reserve System re- [fol. 984] ports each month on the number of workers engaged in these two great groups of industries.

Therefore, we have running back as far as 1919, but not earlier, monthly data, official in character, very carefully compiled, and compiled by several governmental agencies in cooperation, telling us about these groups of workers.

In Table IV, which is on page 9, there appears a list of the durable goods workers by years from 1919 through 1936, and the ton miles of revenue freight of all Class I roads. One can see by looking at those figures that there was a considerable discrepancy between them in 1919 and 1920, and then they get to running in close consonance.

On the following page, which is page 10, there is a diagram, diagram 2, presenting in graphic form the facts that were in that table on the preceding page. Here the solid line shows from 1921 through 1936 the annual figures of revenue ton miles of all Class I roads while the dashed line shows the numbers of workers in the durable goods industries, the workers being in thousands and the ton miles in hundreds of thousands.

There has been a close correspondence throughout the period, a very close correspondence, from about 1925 through 1933, less close in agreement in the past three

[fol. 985] years, and the two lines are now close, more approaching each other.

The assumption in this report is that in the future, as in the past, there would be about 100,000 revenue ton miles of freight carried by our railroads for each factory worker engaged in the durable goods industries when conditions have returned to normal.

There is a way by which we may find out or compute what normal relationships are with regard to these makers of durable goods. We note over a very long term of years there has been very much less variation in the employment of workers in the making of non-durable goods than there has in those of the durable goods, the reason for that being that the non-durable goods includes such things as food, clothing, tobacco, gasoline, and the like, of which we use almost constant quantities in this and in other countries, whether in times of depression or in times of prosperity. So there is a considerable degree of constancy in the employment of those industries even in times of severe depression, as we have just been through.

The durable goods workers that we are talking about in connection with the revenue ton miles greatly increase in numbers in times of real prosperity and seriously suffer from unemployment in times of serious depression.

[fol. 986] On page 14, diagram 3 shows in its upper portion the numbers of factory workers in this country engaged in making durable goods, represented by the solid line, and the numbers making non-durable goods, represented by the dashed line. One notes that the fluctuations of the durable goods solid line are very much greater than those of the dashed line representing the non-durable goods workers. In this diagram the data are entered at the end of the quarter in each year.

In the lower part of the same diagram there is another line showing the percentage of all factory workers engaged in making durable goods.

In such years as those of the long stretch from 1922 through 1929, which in this matter I should consider a period of time including in the main or averaging out to be normal years, the percentage making durable goods turns out to be on the average something more than 51 per cent of the whole.

51.2 is the figure that I have used here.

I now have assumed that the number of workers making non-durable goods in a normal year in this country is 4,200,000. That is the number that were engaged in this kind of work in this past December. It is the number represented by the dashed line in this diagram as of the end of 1936. It is almost precisely the average for that period [fol. 987] from 1923 to 1929.

If we can say that that is the normal number of such workers in this country, and if we can also say that the workers in the durable goods industries represent 51.2 per cent of the total under normal conditions, then we have the figures by which we can estimate the total number of such workers and the number of ton miles of revenue freight to be expected in a normal year. Those figures are presented on page 15 and page 16.

In the paragraph below the table on page 16 the result of those computations is to show that a normal year the total freight revenue at 1 cent per ton mile of revenue freight would be $4,406,557,000.

In recent years the freight revenue has been about 81 per cent of all railway operating revenues of all Class I roads.

Using those figures, it is simple to estimate that on the basis described the operating revenues of all Class I roads in this normal year that we are discussing would be $5,440,193,829, which is a little more than the revenues of those roads in 1930.

At the beginning we said that the operating revenues of this road under discussion has been something more than .63 per cent in 1936 of the total operating revenues of all roads. We had realized that this percentage had been ris- [fol. 988] ing in recent years. I assume in this report we can justifiably believe that in the next year or two or three the relationship will be no less than that. It seems to me that we have reason to believe that the increase that has been running will be continued somewhat further, and that we should expect the Denver & Rio Grande Western to have in a normal year something more than .63 per cent of the operating revenues of all Class I roads.

On that basis, shown in the table on page 17, there are estimates of what the revenues of this railroad might be in a normal year at different fractions of a cent per ton mile. I express here the opinion that with the recent reductions the revenues per ton mile of Class I roads in general

in a normal year are likely to be something like .95 cent. That must be as yet somewhat a matter of opinion. I have worked it out here from 1 cent down to .95 cent.

At 1 cent the indicated revenue of this road from operations in a normal year would be the top figure, $34,273,221; at .95 cent, the bottom figure of $32,559,560.

That concludes the estimates themselves.

I considered further the relative reliability of these estimates, believing that the first figure, that the road should [fol. 989] be expected to earn at least .63 per cent of the operating revenues of all classes of roads, is a reliable figure, which we should expect to be greater rather than less.

Secondly, I believe that the relationship of 100,000 ton miles of revenue freight for each durable goods worker in our factories is of a lesser degree of accuracy, but probably should prove to be pretty reliable in the next few years because of the long history and the fact that the figures are again regaining their old relationships.

Third, I believe that the relationship that says that the workers in durable goods industries tend to be 51.2 per cent of those in all factory industries is probably of a lesser degree of reliability, but my own opinion is that it will prove to be about the same old relationship that it was before the depression.

Finally, the figure of approximately 4,200,000 in the non durable goods industries seems to be a figure of a considerable degree of reliability, although it is a figure already touched in December, and one might argue from that that further recovery might tend to lift it higher.

As to the time, one can only form his conclusion on the assumption that the conditions maintaining and the tendencies under way will continue for the next few years [fol. 990] about as they have in the recent past, unless there intervenes some important unpredictable development like the breaking out of a world war.

On the assumption that there will be no such major development of that sort, it would seem to me that the conditions that I have described here as those of a normal year should have developed in the calendar year 1938, but that the first full calendar year to be a normal year of the sort here considered would probably be 1939, and that the figure that I would give, myself, as the figure for that year for this railroad would be that of $32,559,560, shown on page 17.

By Mr. Nicodemus:

Q. That figure is for the railroad as distinguished from the system?

A. That is for the railroad, yes, as distinguished from the system.

Examiner Kirby: It does not embrace the Denver & Salt Lake?

Mr. Nicodemus: It does not embrace the Denver & Salt Lake.

The Witness: No.

Mr. Nicodemus: It should be compared with Mr. Pyeatt's figure of $30,734,000.

Now we offer the statement in evidence.

Mr. Anderson: No objection.

[fol. 991] Examiner Kirby: The exhibit is received.

(Exhibit No. 121, Witness Ayres, was received in evidence.)

Examiner Kirby: Any questions? Any cross examination?

Mr. Anderson: I would like to ask one question:

Colonel, what would you think would be the effect, upon the whole, of further inflation of credits and currency?

The Witness: It would tend, I think, to lift my figure further above Mr. Pyeatt's.

Mr. Anderson: Also operating expenses, of course?

The Witness: No doubt.

Mr. Anderson: The increase in the use of machinery due to increased costs of labor might reduce the number of people employed in heavy industry?

The Witness: In time.

Mr. Anderson: Yes. That is all.

Mr. Fisher: Col. Ayres, referring to the diagram on page 10 showing the parallel as between the ton miles and the workers in the durable goods industries, the workers' line is about the ton mile line, and the fact that it will approach again the ton mile line is based on the proposition that there will be no further diversion of traffic from railroads to other transportation agencies, is it not? With further diversion of traffic, the ton miles would not parallel [fol. 992] that?

The Witness: That would presumably be true, were it not for the fact that the output of these workers is daily

increasing, the output per man per day. Over this period there has been a steady increase and it has so far, by chance, I think, been just about the amount necessary to offset the diversion of traffic. As long as those trends continued in about those proportions, the relationships will maintain, but should they change, of course, that would not longer be so.

Mr. Fisher: You do not consider that the divergence between those two lines that have taken place since early in 1933 is due to diversion of traffic to trucks, etc.?

The Witness: I do not, no. I think those lines are going to close together again and be about as they were before.

Examiner Kirby: Any further questions?

Mr. Nicodemus: You are excused.

Examiner Kirby: If the record does not show, exhibit 121 is received in evidence.

* * * * * * *

[fol. 993] WITNESS WILLIAM WYER

Q. Now, the Examiners requested an Exhibit with respect to working capital. Have you prepared such an Exhibit?

A. Yes, sir. Mr. Boyden asked me if I could give an estimate as to the amount of working capital required by the new company, and I have prepared an exhibit based on that subject.

Q. Will you describe the exhibit?

A. This exhibit is in one sheet and is headed, "Cash in hands of Treasurer last day of each month 1926, 1935", and you will note from that it has fallen as low as $260,000 on the last day of March in 1935, and it has been as high as $7,120,000 the last day of November, 1929.

Now, the second half of this exhibit shows the cash on hand of various railroads in the Western District as of December 31, 1935. I have excluded railroads which were in Trusteeship. These are railroads not operating under the jurisdiction of any court.

I feel as to the amount of working capital—and these figures which I have presented on the exhibit have had some influence on my answer, as well as my own experience with the Denver—that the working capital should never fall [fol. 994] below $1,000,000, and that it would be much better if it could be in the neighborhood of $4,000,000 or $5,000,000; as far as the plan is concerned, we do not know how

much cash the new company is likely to start with, because we cannot forecast the operations of the Trustees. We would assume, the way the plan is drawn, that we would start in with the cash, operating cash, which the Trustees have, but because of the uncertainty as to what that is likely to amount to, I feel that the amount of treasury bonds should be reasonably large so that if the trustees should happen to turn the property over at a time when the cash was nearer the one million dollar mark than it was the four million dollar mark, that we would be protected as to working capital.

Examiner Boyden: Is that estimate of working capital for the proposed new corporation, the consolidated and reorganized company?

The Witness: Yes. I would place the limits at somewhere between one million dollars and five million dollars for the new consolidated company, including the Denver and Salt Lake. These figures here, of course, are just for the D. & R. G. W., on Exhibit No. 124.

Examiner Boyden: If you can permit your cash to run as low as one million dollars, what would be the need for providing as high as five million dollars cash?

[fol. 995] The Witness: Well, what you need a higher figure for is this:

When you are making Additions and Betterments to your property, if you have to borrow for any of those Additions and betterments, you do not want to be in the position where you have to borrow every time that you decide to make an improvement. We want some cash to put into Additions and Betterments, with the idea that when that amount has reached a large enough figure, you will be in position to sell some bonds, and you have to have some leeway there.

Of course, if you were to operate this property and pay for all your Additions and Betterments out of income, and never have to borrow, you could get along on a smaller amount of working capital than you could otherwise, but there are things like that which have to be taken care of currently, and when you cannot go out and reimburse yourself currently.

Examiner Boyden: Under your plan of reorganization, which provides for various sinking funds, would not the matter of Additions and Betterments be taken care of, and

under those circumstances would not a one million dollar figure be sufficient?

The Witness: They would be taken care of to a great deal better extent than they have been in the past. I do not [fol. 996] believe they would be fully taken care of. I would expect that there would be some occasions when you would have to be borrowing for Additions and Betterments.

[fol. 997] By Mr. Fooshee:

Q. Representing the Guaranty Trust Company of New York as Trustee of the Rio Grande Western Railway Company First Consolidated Mortgage, (RGW Consols) due 1949.

Mr. Wyer, the Plan proposes that the Utah Fuel stock which is now pledged, the total of that stock which is now pledged under the Denver & Rio Grande Western Consolidated Mortgage as a first lien thereon shall be placed under the general income mortgage as a first lien, does it not?

A. Yes.

Q. Is there any other attribution of income to the Utah Fuel Stock other than the $83,333 shown in exhibit 107, I think it is, which was taken on the basis of being a dividend of $250,000 cash paid in 1934 and distributing that dividend [fol. 998] over three distribution years, 1932, 1933, and 1934?

A. There is no other attribution of income to that stock.

Q. Yes. Has there been a valuation of the properties of the Utah Fuel Company made for purposes of this reorganization plan?

A. No, there has been no appraisal or valuation made specifically for this purpose.

Q. Exhibit 36 states that the property of the Utah Fuel Company was valued on its consolidated balance sheet as of December 31, 1935, at $15,118,543, less reserves of $3,149,875.

The properties are ~~value at that on~~ the balance sheet; how was that carried, was that carried at cost, that is page 2 of exhibit 36?

A. I cannot tell you definitely how that figure originally came onto the balance of the Utah Fuel Company.

Q. I thought it was in the record, although I was unable to place my hand on it, in response to a prior question, that

it had been cost of the properties to the Utah Fuel Company.

A. Well, that is my impression, but I am not entirely certain as to that.

Q. The stock of the Utah Fuel Company was sold pursuant to the levy on the judgment of the Equitable Trust Company in 1918, wasn't it?

[fol. 999] A. Yes.

Q. Do you recall at what amount that stock was bought in, was sold for?

A. No, I do not.

Q. You do not recall that it was approximately ten million dollars; that would not refresh your memory? I do not want to make that statement.

A. I think that is correct. I am willing to accept your statement on that.

Q. So that the equity in that stock, the equity in that stock is pledged under this Denver & Rio Grande Western Consolidated mortgage?

A. I think it was. That is going back a long ways and is something that I have not looked into for a long time, but I think there was some debt outstanding ahead of the stock at that time; I do not recall just how much.

Q. It might refresh your memory if I should point out that exhibit 36, page 1, shows that on June 30, 1918, the equity in the stock owned by the Denver & Rio Grande Western was sold under a decree, without stating the amount for which it was sold, and that that page also states that all of the stock was pledged under the Denver & Rio Grande Western First Consolidated Mortgage by indenture dated May 23, 1901—that is 17 years, approximately, before that—I do not know whether that would refresh your recol-

[fol. 1000] lection on the point of letting you say that that equity was the equity remaining after the pledge of the stock to the Denver & Rio Grande Western Consolidated.

A. Well, what I had in mind was that there were some debts of the Utah Fuel Company outstanding and when I said the equity in the stock——

Q. Yes.

A. I had in mind that debt.

Q. Yes.

A. No, of course, the sale at that time was to somebody who expected to own the D. & R. G. and the pledge under

the R. G. W. Consols would not be ahead of the equity, I would not think, as a business proposition, under those circumstances, I would not expect that pledge to come ahead of the equity remaining in the stock at that time.

That is, those bonds would be outstanding against the D. & R. G. property in the same amount, anyway, I should think.

Now, I might not be entirely correct as to that, but I did not, at any rate, have in mind that the pledge to the R. G. W. Consols came ahead of the equity for which ten million dollars was paid in 1918.

Q. Well, you do not know that that pledge made in 1901 was not a pledge, an existing pledge at the time the stock [fol. 1001] was sold?

A. No, I know it was.

Q. You know it was?

A. Yes.

Q. That is sufficient on that, I think.

The earnings, the consolidated income account for the Utah Fuel Company is shown only for the years 1930 to 1935, inclusive?

A. Yes.

Q. Do you know whether the earnings of income as shown in exhibit A, and exhibit 36, are representative of the income for the years immediately preceding 1930?

A. Oh, I think their earnings were a little better prior to 1930 than they were during these years.

Q. Had one of the large purchasers of coal, namely, the Missouri Pacific, cut down the amount of its purchases in 1930?

A. Yes.

Q. From what they were prior to that?

A. It had.

Q. That is the same Missouri Pacific Railroad, isn't it, that is one of the two roads which under the plan would retain the common stock of this company?

A. Yes, that or the successor company.

* * * * * * *

[fol. 1002] By Mr. Hoffman:

Q. Are you willing, for the purpose of this record, to accept Colonel Ayres' testimony that 1939 is a normal year, or will be a normal year?

A. Yes.

Q. Are you willing, for the purpose of this record, to accept Mr. Pyeatt's testimony with respect to the forecast of earnings for a normal year?

A. Yes.

[fol. 1003] Q. What is your definition of "a normal year?"

A. "A normal year" is the year which represents an average condition that you can expect in the future, and I would expect earnings in the future to run considerably above or considerably below the normal year.

Q. So that a normal year would, on the average, take into account the peaks and valleys of earnings, profits as well as deficits? Is that right?

A. Yes.

Q. And a normal year would mean that if you took a reasonably representative period of earnings and losses, a large number, whatever they may be, you should arrive at approximately that figure which we call a normal year's earnings. Is that right?

A. That is what I would understand about it.

. . . . . .

[fol. 1004] WITNESS WILLIAM WYER

. . . . . .

Q. $6,700,000. On the basis of earnings for the test period, there were no earnings for the common stock, were there? The test period.

A. No.

Q. On the basis of the normal year there were no earnings for the common stock, were there?

A. On the basis of Mr. Pyeatt's estimate for the normal year, there are no earnings for the common stock.

. . . . . .

[fol. 1005] Q. What do you give them for their equity in the Utah Fuel?

A. We do not consider that there is any equity in the Utah Fuel at the present time.

Q. No equity in assets?

A. No equity on the basis which we have appraised it in connection with the Utah Fuel in this plan.

[fol. 1006] Q. No equity in either assets or earnings?

A. No.

Q. You consider the Utah Fuel as worthless?

A. No, we have made an allowance to the R. G. W. 4's of 1949 for their lien on the Utah Fuel. We think that has absorbed the whole value of the Utah Fuel.

Q. On the basis of earning power?

A. If we had done it on the basis of earning power, it would have been, yes. The Utah Fuel has not had any earnings for five or six years.

Q. And on the basis of asset value?

A. On the basis of book value it has a very substantial value, but I do not know what good that is to you, if you are earning deficits all the time.

Q. Have you any opinion yourself as to the value of the Utah Fuel stock?

A. Not in dollars and cents, but I have a general opinion on it.

Q. I mean in dollars and cents.

A. I have not attempted to set an exact value on the Utah Fuel stock.

Q. Have you an approximate figure in mind?

A. No.

Q. Any figure which you can mention, by which we may guide ourselves here?

[fol. 100.] A. No, I have tried to present all the facts about the Utah Fuel Company here and all the basis on which we appraised it for the purpose of the plan, and that is as much as I can say by way of an exact figure.

Q. If I may summarize it, we will take $83,000 of income as being an amount which we will attribute to the Utah Fuel, and that is how we will deal with that stock under the various mortgages which may be entitled to it. That is about the substance of it?

A. That is where we arrive, after considering all the factors.

Q. That is about the substance of it?

A. That is not the substance of all the information which we have put in about the Utah Fuel Company.

Q. It works out that way?

A. Yes, sir.

* * * * * * *

[fol. 1008] J. S. Pyeatt testified further as follows:

Direct examination (Cont.):

The Witness: I have a few corrections which I would like to make in the previous record. They are quite brief, and I can read them.

Examiner Boyden: Is it not satisfactory to put them into the record?

The Witness: Yes, it is satisfactory.

Examiner Boyden: Will you offer the exhibit, please?

The Witness: Page 808, line 15, the word "figure" should be "annually".

Page 813, line 20, insert "owned" after "number".

Line 21, the figures "6.5" should be "5.5".

Line 22, "6.7" should be "6.9".

Page 835, line 22, the word "revenue" should be "rental".

Page 836, line 2, the word "traffic" should be "trackage".

[fol. 1009] At the previous hearing Exhibit No. 117 was presented showing, among other things, estimated net and gross ton miles for the normal year. After that exhibit was submitted, we discovered a mistake arising out of the figure for the average haul, which we took to be 240 and it should be 249. That resulted in a change in the gross ton miles for the normal year of 7,228,028,000 in place of 6,966,792,000, a percentage of increase of 3.75.

Net ton miles of 2,659,282,000 instead of 2,563,173,000.

By Mr. Hodges:

Q. Mr. Pyeatt, have you prepared an exhibit marked 117-A to submit, showing the corrections in Exhibit No. 117?

A. No, we have just made this correction.

Q. This document? (Producing paper.)

A. Yes.

Examiner Boyden: Do you offer it for the record?

Mr. Hodges: We offer it for the record.

Examiner Boyden: It is received as Exhibit No. 127.

Mr. Hodges: It is marked Exhibit No. 117-A.

Examiner Boyden: I understood you were correcting Exhibit No. 117-A.

Mr. Hodges: Correcting Exhibit No. 117 by Exhibit No. 117-A.

Examiner Boyden: We will receive it, then, as Exhibit No. 117-A.

[fol. 1010] (Exhibit No. 117-A, Witness Pyeatt, received in evidence.)

By Mr. Hodges:

Q. Does Exhibit No. 117-A show all the corrections which are necessitated in Exhibit No. 117?

A. As to gross and net ton miles.

At page 838 of the record Mr. Hoffman requested the total amount of improvements and maintenance charges in connection therewith during the period when no interest was paid on general 5's, February 5, 1924, to January 21, 1929, and from date of default of Refunding and Improvements or the Generals, whichever was first, down through 1936.

We have that exhibit.

Mr. Hodges.: What is the number of that exhibit? We offer that exhibit in evidence.

Examiner Boyden: It will be received as Exhibit No. 127, if there is no objection.

(Exhibit No. 127, Witness Pyeatt, received in evidence.)

Mr. Hodges: That is a new exhibit and will take a new number.

Examiner Boyden: It is received as Exhibit No. 127.

Mr. Hodges: Anything further, Mr. Pyeatt?

The Witness: Yes. In our estimate of taxes there appears an item of $2,700,000 for the normal year to cover [fol. 1011] taxes. Unfortunately, the memorandum which we took that from did not include the income taxes and undistributed profits taxes. That amounts to approximately $350,000, income taxes, and $75,000 on undistributed profits taxes for the Denver & Rio Grande Western and $97,000 for income taxes, and $93,000 undistributed profits tax, estimated, of course, for the Denver & Salt Lake.

Examiner Boyden: For what year is that, Mr. Pyeatt?

The Witness: That is for the normal year, estimated. That is not the total items because the amount of $2,700,000 was somewhat above the estimate of the total items, but if the A. and B. fund is not used to run through depreciation and appropriating for additions and betterments, that would result in a deficiency in taxes under our estimate of $225,000

on the D. & R. G. W., and approximately $172,000 on the Denver & Salt Lake, or a total of $397,000.

But if, as I assume may be done, there is a charge to depreciation and maintenance of way to cover expenditures for additions and betterments, and we use the depreciation for the additions and betterments to the extent appropriated for that, that would result in a deficiency of $16,000 for the Denver & Rio Grande Western in our estimate as made, and $159,000 for the Denver & Salt Lake, or a total of $175,000.

* * * * * * *

[fol. 1012] Q. Mr. Pyeatt, on page 821 of the record I am going to read what you said, because I think it is an error in transcribing, and I would like to get it straight before I go ahead. At page 821 of the record, in reply to a question, "What is meant by a normal year", I refer to an answer that begins at the bottom of page 820. In reply to the question, "What is meant by a normal year", your testimony, as transcribed, reads:

"It is the year when occur all of the flush or unusual traffic movements to take care of the lack of construction of all sorts, and the lack of activity during the depressed period."

Is that correctly transcribed?

A. I think it may be correctly transcribed. If the meaning of it is not clear, I would like to say that it is the time after all of these deferred things and the extraordinary activity by reason of them have occurred.

[fol. 1013] Q. Would this temporary intervening period of flush or unusual traffic, to be followed by a dropping back a little way to normal, be experienced equally in the case of every class of commodity?

A. No, I would not think so.

* * * * * * *

[fol. 1014] By Examiner Kirby:

Q. Mr. Pyeatt, will you please refer to your exhibit 118?

A. I haven't these exhibits numbered.

[fol. 1015] Q. That is the data study?

A. Yes.

Q. Page 2. In arriving at your total freight revenues for the normal year, that is, your forecast?

A. Yes.

Q. Have you made any deduction or correction for switching absorptions and corrections?

A. No, sir; this is the total revenue, including switching. We cut that out, this is the net.

Q. Well, your data for the period seems to indicate that you did make deductions in the use of the data, and is the explanation of this that having made the deductions in the data, you therefore arrive at the net result without making any further deductions in your forecast?

A. Yes; this is the total revenue after any payments or collections that we may make, as I understand it.

Q. No further deduction is necessary, then in your forecast?

A. No.

Q. Is that correct?

A. That is correct.

Q. Now, throughout this exhibit, 118, have you in all instances applied a revenue rate per ton?

A. Yes.

Q. In the forecast, which does not reflect the increases [fol. 1016] due to emergency surcharges.

A. Well, increases we thought would be made were considered in that. We do not know what they would be, but we felt that the present hearing on that would result in a material increase in certain commodities.

Q. In other words, you are anticipating increases in the rates?

A. Yes, to some extent.

Q. In the figures, though, extending over the eight-year period, there are reflected in the revenues per ton for the last year or so, the effect of the emergency surcharges, are there not?

A. That is correct.

Q. In applying the averages per ton derived from this basic data, have you made a compensating adjustment for the effect of the emergency surcharges?

A. No, I do not think that we did. I think we took into consideration that the surcharge would be canceled and that as result of the hearing now in progress, that a great many of those rates would be restored.

Q. Which hearing are you referring to?

A. Well, the application for increases in rates.

Q. So, in effect, you have left in the influence of the emergency surcharges, have you not?

A. Yes, I think we took the rates existing up to the last [fol. 1017] date available, 1936, and considered those rates in connection with the rates of previous years and what we thought they might be in a normal year.

Q. You have not used a straight average over the years, however, have you, for the revenue per ton?

A. No.

Q. Well, now, just one or two questions covering quite a number of items.

I notice that in the application of the revenue per ton in your forecast, the rate on individual commodities in several instances coincides with the average revenue per ton for 1935, and in some of those instances the 1936 revenue per ton for the entire year 1936 is less than the 1935 rate.

You did not have the full year available at the time you made up this exhibit, did you?

A. No, I think we had about nine months.

Q. And we have now asked Mr. Wyer to supplement that commodity statement so that we will have the results for the full year 1936. That might in some cases change the average for the nine months which you have shown, would it not?

A. It might.

Q. In those cases where the 1936 revenue per ton is considerably less than the 1935 revenue per ton, would you [fol. 1018] still claim that the application of the 1935 rates in your forecast is proper?

A. Well, I think we took into consideration the rates running over the eight year period here, and the fact that there is a variation in the rates on many commodities every year, every six months, to put in an estimated rate for the normal year that was felt to be fair reflection of what it would be. Of course, it is an estimate, a guess.

Q. It is a judgment figure?

A. Yes.

Q. However, I won't pursue it further except to ask you this question: On lumber, shingles, and lath, on page 91, your forecast rate per ton is $2.73 and the 1935 rate is $2.73; there they coincide?

A. Yes.

Q. As a matter of fact, the 1936 rate is only $2.63; that is to be developed from the information to be furnished?

A. That is correct, and by the same token, the rate for the first nine months of 1935 was $2.70 as against $2.73 for the year, so that does vary a good deal according to the movements, the destination.

Q. I notice that the 1936 rate was somewhat less, $2.63. Would that cause you now to change the rate which you [fol. 1019] applied in the forecast for that particular item?

A. No, I do not think I would change that. Lumber was one of the commodities that we estimated might be increased as result of the present application.

. . . . . .

[fol. 1020] Q. You have been asked by Examiner Kirby about your treatment of emergency surcharges. I direct your attention to your exhibit 118 and ask if you have not eliminated the effect of the emergency surcharges in some instances, calling atteniton to pages 130, 128, 123, 120, 118, 114, 108, and 80.

A. I do not understand so. I do not——

Q. I call your attention first to page 130. Will you look at it, please? First, as to tractors and parts, ICC Classification No. 582; the bottom note says; "Average revenue per ton based on present levels less the emergency increase," I just want to be sure that I don't misunderstand what that means.

A. Yes, that clearly states that it is on present levels.

Q. Where there is such a notation, that is the meaning of [fol. 1021] it, is it not?

A. Yes, I assume so. I did not put in any of those figures. They were all figured in Mr. Wyer's office and in our consideration of the revenues and expenses in that meeting that we had in Chicago with Mr. Brown and Mr. Taylor at that time, we did not make any chances on account of emergency rates because it hadn't then been cancelled.

Q. Well, I will call your attention to page 128 of your testimony, you haven't it before you, I will read a question that was propounded to you then by Mr. Fisher:

> "Did I understand you to say that you started off on the basis of complete loss of surcharges, plus the increased rates on certain commodities and what you

felt was reasonable expectation of obtaining in Ex Parte 115?"

"The Witness, yes."

Shall we alter that in any way in view of your present testimony, or does that stand as being the process of arriving at these forecasts?

A. Well, it appears to need altering in view of my two statements of it. We made our first statement in December. That was brought back in carloads, and the tons, the rate per ton and the revenues were figured in Mr. Wyer's office. [fol. 1022] And I think it is better to state that I was perhaps not as well informed on that as I should have been, and that I was not sure of it except that we did not give consideration to the elimination of the surcharge in December when we made up our first figures. We apparently have in this final draft.

* * * * * * *

[fol. 1023] T. A. Hamilton, was sworn and testified as follows:

Direct examination.

By Mr. Clay:

Q. Will you give your name for the record, Mr. Hamilton?

A. T. A. Hamilton; residence, Houston, Texas.

Q. State briefly your previous qualifications and experience.

A. I began railroading in 1916 as telegrapher on the Canadian Pacific. I have spent some forty years in active railroad service and in employment directly related. In [fol. 1024] my railroad experience I have served as telegrapher, station clerk, bill clerk, chief clerk to Superintendent, Yard Master, Chief Clerk to General Manager, Assistant General Manager, Assistant to Operating Vice President, Assistant to the President, Vice President in charge of operations, Vice President and Comptroller and President.

My service has been with the Canadian Pacific, Chicago and Grand Trunk, Missouri Pacific, Illinois Central, Louis-

ville and Nashville, St. Louis-San Francisco, International Great Northern.

I left the Operating Vice Presidency of the St. Louis-San Francisco to take the Presidency of the International-Great Northern, at its reorganization in 1922, and remained in that capacity until its sale to the New Orleans, Texas and Mexico and its absorption into the Missouri Pacific System.

Since that time I have been engaged in consulting work, inspections of railroad properties and matters of that kind for various banking interests.

In August 1934 I joined the Railroad Division of the Reconstruction Finance Corporation as an Examiner and engaged principally in outdoor work, field work, and am still in that employment.

Q. What is your first exhibit, Mr. Hamilton?

A. A map of the Denver and Rio Grande, The Denver and [fol. 1025] Salt Lake and the Denver and Salt Lake Western, which are separately colored for purposes of easy identification.

Mr. Clay: I would like to offer this map as Exhibit No. 129.

Examiner Boyden: It will be marked Exhibit No. 129, for identification.

(Exhibit No. 129, Witness Hamilton, was marked for identification.)

By Mr. Clay:

Q. Would you state what inspection you have made of this property recently, Mr. Hamilton?

A. I made a daylight inspection in company with the Maintenance Engineer of the Denver and Rio Grande Western of the line of that road, from Denver via Pueblo to Dotsero on May 12th of this year, and of the Denver and Salt Lake Western and the main line of the Denver and Salt Lake, from Dotsero to Orestod and Orestod to Utah Junction, Denver, on May 13th. I subsequently followed the line of the Denver and Salt Lake from Steamboat Springs into Utah Junction, on May 22nd, in company with the Chief Engineer of that property.

Q. Looking at this map, would you define for the purposes of your testimony the stretch of line which is marked in red? How will you describe that?

[fol. 1026] A. That is the Denver and Salt Lake Western, known as the Cut-off.

Q. You mention it as the Cut-off?

A. Yes, sir, for easy reference, the Cut-off.

Q. And the line from Bond to Denver?

A. Yes, sir. The Denver and Salt Lake Railroad, one of the railroads which we have termed the Moffat route.

Q. That leaves only one other mileage?

A. The combination of those two we have spoken of as the Cut-off-Moffat route, for the sake of easy reference.

Q. How about the line from Bond to Craig?

A. That is from Orestod, if you will pardon me, to Craig, referred to as the Denver and Salt Lake, and specified in each reference as the line north of Dotsero or between Orestod and Craig.

Q. What are your next exhibits?

A. I have the profile of the main line and of the Denver and Rio Grande Western from Denver to Ogden, of the Denver and Salt Lake Western from Dotsero to Orestod, and the Denver and Salt Lake from Orestod to Denver or Utah Junction.

In connection with that I have in tabular form a description of the alignment and the grades on the mileage re-[fol. 1027] ferred to in the profile.

Examiner Boyden: Mark the map Exhibit No. 130 and the tabulation Exhibit No. 131.

(Exhibits Nos. 130 and 131, Witness Hamilton, were marked for identification.)

Mr. Clay: I would like to offer these two exhibits.

By Mr. Clay:

Q. Will you please comment on Exhibits Numbers 130 and 131?

A. One is explanatory or explains the other. The second one is a statement in tabular form of the profile.

The purpose of the exhibits is to show the handicaps of adverse grades and curvature encountered respectively, on the route over Tennessee Pass, that is Denver via Pueblo to Dotsero and beyond, and the Cut-off route.

In moving traffic westbound from Denver to Dotsero via the Tennessee Pass route, that is, via Pueblo, we find 181.14

miles of opposing grade, as compared with 52.44 miles of opposing grade westbound over the Cut-off-Moffat route.

Q. Will you give more detail on those grades?

A. Yes, sir, I was about to do so.

Of eight-tenths and less there are 86.6 miles on the Ten- [fol. 1028] nessee pass route and 10.70 on the Cut-off-Moffat route.

Over eight-tenths and up to and including 1 per cent, 37.10 miles via the Tennessee Pass route and 1.87 miles via the Cut-off-Moffat route.

Over 1 per cent to and including 1-1/2 per cent, 55.6 miles via the Tennessee Pass route and 5.27 miles via the Cut-off-Moffat route.

Examiner Boyden: Just a minute, Mr. Hamilton. You say over one, What was the last class which you read?

The Witness: Over 1 per cent to and including 1-1/2 per cent.

Then over 1-1/2 per cent to and including 2 per cent, 1.84 miles via the Tennessee pass route and 34.60 miles via the Cut-off-Moffat route.

By Mr. Clay:

Q. That is the movement westward from Denver to Dotsero?

A. Yes, sir, that is opposed to westbound traffic.

Q. How about on eastbound traffic?

A. Pardon me, I might say, parenthetically, the heavy freight movement over both routes is preponderantly eastbound.

The grades opposed to eastbound traffic are eight-tenths of 1 per cent and less 57.30 miles via the Tennessee Pass route and 70.37 miles via the Cut-off-Moffat route. Over [fol. 1029] eight-tenths to 1 per cent, and including 1 per cent, 24.20 miles via the Tennessee Pass route and 13.39 miles over the Moffat-Cut-off route.

Over 1 to and including 1-1/2, 30.15 miles via Tennessee Pass and 2.94 via the Cut-off.

Over 1-1/2 to and including 2 per cent, 3.30 miles via the Tennessee Pass and 5.10 miles over the Cut-off-Moffat route.

Over 2 per cent to 2-1/2, .44 miles over the Tennessee Pass route. There are no grades above 2 per cent eastbound on the Cut-off-Moffat route.

Over 2-1/2 per cent to 3 per cent, Tennessee Pass Route, 11.80 miles and over 3 per cent .40 miles.

The total miles of opposing grades, that is, grades opposed to Eastbound traffic over the Tennessee pass are 127.59 as against 91.80 over the Cut-off-Moffat route.

Q. In other words, on eastbound traffic there is a striking advantage for the Cut-off-Moffat route over the Tennessee Pass route?

A. Yes, sir, and those are the grades opposed to the preponderantly heavy traffic.

The amount of level line on the two routes is 34 miles via Tennessee Pass and 22.47 via the Cut-off-Moffat [fol. 1030] route.

As to distance, the total distance between Dotsero and Denver is 175 miles shorter via the Cut-off-Moffat route than over Tennessee Pass.

Q. Pardon me, is that 175 or 176?

A. 175, sir.

Based upon the figures which I have quoted from the profile and the company tabulation, it is apparent that the most advantageous route for freight traffic, and incidentally for passenger traffic, but especially for freight traffic, of which the preponderant volume is eastbound, is over the Cut-off-Moffat route.

Q. That is so far as grades are concerned. Will you comment now on curves?

A. Yes, sir. A comparison of the curvature on the Tennessee Pass and the Cut-off-Moffat routes is:

5 degrees and less, Tennessee Pass route 96.81 miles, Cut-off-Moffat Route 39.73 miles.

Over 5 degrees to and including 7, 21.36 miles and 18.63 miles respectively.

Over 7 degrees to and including 8, 2.81 via Tennessee Pass and 2.23 via the Cut-off-Moffat route.

Over 8 degrees to 10 degrees, 3.30 miles via Tennessee Pass and 10.50 via the Cut-off-Moffat route.

[fol. 1031] Over 10 degrees to and including 12, 2.69 miles via Tennessee Pass and 7.69 via the Cut-Off-Moffat route.

Over 12 degrees to 13 degrees, 1.96 miles Tennessee Pass and 2.20 via the Cut-Off-Moffat route.

There is no curvature on the Tennessee Pass route above 13 degrees. On the Cut-off-Moffat route there is .9 miles ranging from 15 to 16 degrees and .14 of a mile with a curve of 16 degrees and 36 minutes.

I might say, in setting up this table, or in quoting the figures which I have put into the record, we have dropped everything below 30 minutes, and kicked up everything above, in rounding out the degrees.

Q. This information was obtained from the track charts of the railroad?

A. From the Engineering records of the railroad, yes, sir. The Tennessee Pass route has 58 per cent more mileage than the Cut-off route.

There is an excess on the Moffat route of curvature of over 8 degrees.

When I went to look at the property, I heard a great deal about one-sixth degree curvature on the Moffat route, and found, when I came to see it, there was 23 100ths of a mile [fol. 1032] in the aggregate, and I saw one of the curves, the longer one, which was in process of reduction to twelve degrees, the last day I was on the railroad.

Q. Referring to Exhibit No. 150, how did the two roads compare with reference to the highest point, that the road has to cross?

A. The summit at Tennessee Pass is approximately 2000 feet higher than the apex in the Moffat tunnel.

In connection with the grades that we have been talking about, it may be of interest to state what helper service is operated.

Eastbound from Minturn on the Tennessee Pass, the summit, helper service is operated the entire distance of 21 miles on freight trains.

On the other side of the pass, going up from the gorge westbound, helper service is not operated although the grades run pretty close to 1.4 per cent.

On the Moffat line from Tabernash through to the East Portal of the tunnel helpers are regularly employed. The district is about 16 miles. Westbound from Denver to the East Portal of the Tunnel helper engines are employed over a 50 mile territory whenever the tonnage of the train exceeds the rating of a single locomotive. Our examination of train sheets for a representative period indicates that [fol. 1033] that was the case about half the time. That is, about one-half of the trains had to be helped up.

Q. Comparing the helper service on the two lines, would you characterize one as the most burdensome helper service, or, rather, on which there is a need of more helper service?

A. You have got a long stretch of 1.4 per cent grade up the east side of Tennessee Pass, that is, up to the summit, on which there is no helper service, and of course they have to help up the 3 per cent grade eastbound on the other side of Tennessee Pass, and there is helper service on both sides of the Moffat Tunnel. The fact that helpers are not operated westbound up the Tennessee pass of course lightens the train load.

Q. What is your next Exhibit?

A. I have an Exhibit here which shows the rail and ballast characteristics of the two routes, that is, The Tennessee Pass Route and the Cut-Off-Moffat route.

I also have an exhibit which describes the tunnels.

Q. May I interrupt a moment?

A. Yes, sir.

Mr. Clay: May it please the Commission, we have the Exhibits here which I think would best be discussed in rela- [fol. 1034] tion to each other.

By Mr. Clay:

Q. What is the next exhibit?

A. This describes the tunnels between Denver and Orestod and Pueblo and Dotsero, and Dotsero and Orestod and third the bridging on the routes.

Examiner Boyden: Mark the statement of rail and ballast characteristics, 132, and the description of tunnels No. 133, and the Bridge Exhibit No. 134.

(Exhibits Numbers 132, 133 and 134, Witness Hamilton, were marked for identification.)

Mr. Clay: I would like to offer these three exhibits.

* * * * * * *

[fol. 1035] T. A. Hamilton testified further as follows:

Direct examination (Continued).

By Mr. Clay:

Q. You were just starting to comment on Exhibit No. 132, 133 and 134?

A. Yes, sir.

The first of the three exhibits, that is 132, shows the miles of the various segments, weights of rail in the main track, in the second main track, on various sections of the Denver and Rio Grande Western between Denver and Ogden. The track between Denver and Pueblo is paired with the Atchison, Topeka and Santa Fe for operations, a total of 102.9 miles.

The rail and ballast characteristics, which are also included in the Exhibit, describe the Denver-Pueblo mileage, those of the Denver and Rio Grande Western track in paired arrangement.

The same exhibit compares the rail and ballast character- [fol. 1036] istics for the Denver and Salt Lake Lines, the Moffat Line, between Denver and Orestod, the part over which the Denver and Rio Grande Western now operates under trackage rights.

There is a similar description for the line between Orestod and Dotsero of the Denver and Salt Lake Western, which we have been terming the Cut-off. The main line of the Denver and Rio Grande Western between Denver and Dotsero is in pretty good shape. There have been substantial rail renewals, tie renewals, bridge renewals and strengthening and a pretty good ballast job. In nothing that I am going to say about these physical characteristics of the two routes do I mean to imply that the track over Tennessee Pass, that is the line from Denver to Dotsero via that route, is not a good railroad; it is very good railroad. And the data in this rail and ballast chart indicates that. Rail and ballast, I should have said table, instead of chart.

However, the line from Denver to Orestod, the Denver and Salt Lake, is or will be within a few months a practically new railroad. It is being laid now with 100 pound rail complete throughout, and that job will be finished, we are told by the engineering forces, sometime in July of this year.

[fol. 1037] Along with that rail laying job is a complete necessary tie renewal and a job of ballasting, principally with volcanic cinders, which will make a first class railroad out of it.

The ballast job is complete now, with the exception of eleven miles, which will have to be done gradually because of having to dig down in the tunnels to maintain overhead clearances and because of some necessary work to be done

on the track approaching the tunnels in the same connection.

During the current year that job should be completed, so that the Denver or rather Utah Junction—Orestod line will be a first class railroad in another month, or two or three at the outside.

We have discussed, or I have described, rather, the gradient and curvature characteristics of the line and the only two sixteen degree curves, which have somewhat obscured the proper viewpoint of the rail alignment on the road are now disappearing, one is being taken out currently and the other is programmed for the near future.

As to the tunnels on the line, which Exhibit 133 describes, there are 39 tunnels on the line between Utah Junction and Orestod, of a total length of 18,020.0 linear feet, of which 8,102.0 feet are timber lined and 9,918.0 are unlined rock [fol. 1038] bore. These figures do not include the Moffat Tunnel.

It is a fact that the timber lining in the tunnels between Utah Junction, and Orestod, excluding the Moffat Tunnel, which is not timber lined, are not in very good shape. Some relining is under way now, and a practically complete job is programmed for the next two or three years.

Even if the linings are replaced entirely with concrete, the total cost would not exceed $120,000 for the entire job.

The Moffat Tunnel of a total length of 32,798 feet, is concrete lined for 18,231 feet and Gunnite lined for 14,567 feet, with a good state of maintenance as to lining.

Trackage conditions in the tunnel are good with one exception. A deposit of soot and cinders on the western side of the apex of the tunnel has made lining and surfacing conditions difficult. This material is mixed with the ballast so that the track put up apparently solidly today is down again tomorrow or within two or three days.

The work of removing this material, this debris, if you want to call it that, from the tunnel, is programmed for the next 30 days and with the better ventilation that now obtains, better than in the past, it is believed that this trouble will not recur. With that exception and the retirement of the timbers of the tunnels at a cost of about $120,000, maxi- [fol. 1039] mum, there is no deferred maintenance or future maintenance in sight as far as tunnels are concerned.

As to the Denver and Salt Lake Western, the cut-off, of course this is a brand new railroad, opened for operation

June 14, 1935. It is laid practically throughout with relay 90 pound rail, and the remainder with new 90 pound rail.

The rail is in present good condition. There is no reason why it should not serve satisfactorily for a good many years to come under the present, or even a substantially increased traffic volume. 90 pound rail is somewhat outmoded these days, but there are still in the west a good many thousands of miles of 90 pound rail, of which I have had recent personal opportunity to inspect in heavy traffic trunk lines that still has a good deal of life in it. I am thinking particularly of the Chicago, Milwaukee, St. Paul & Pacific on the west end and some of the principal secondary main lines and part of the primary main lines of the Great Northern.

The construction of the Denver & Salt Lake Western, or the cut-off, is an excellent job of work. Its very good alignment was secured in a very difficult territory, much of it by substantially changing the channel of the Colorado River. The road is built with native rock, all of the em- [fol. 1040] bankments, or practially all, are made of rock, are wide, amply sloped and just about as durable as that class of work can be.

The material in the railroad, with the exception of the relay 90 pound rail, is all new. It has been seasoned pretty well under traffic since it was opened for operation in 1935 and is today in good condition.

It does not present any maintenance problems.

The tunnels on this line consist of two, with a total of 1762 linear feet concrete lined, and at present in good condition.

I neglected to speak of the tunnel condition of the line between Denver and Dotsero, via Pueblo. There are no tunnels between Denver and Pueblo. Between Pueblo and Dotsero there are 2577.0 feet of timber lined tunnels, 585.5 feet of concrete lined and 991.0 feet of unlined rock bore.

Examiner Boyden: Mr. Hamilton, all that material is in the exhibit?

The Witness: Yes, sir.

Examiner Boyden: Mr. Clay, why, if it is in the exhibit, unless there is some particular thing to which attention is to be called, why go into the detail in oral testimony?

Mr. Clay: Could you leave out some of the detail, Mr. [fol. 1041] Hamilton?

A. Yes, sir.

Q. Confine yourself to a comparison of the two roads.

A. The condition of the tunnels between Pueblo and Dotsero is good, with the exception of one, Tennessee Pass, the repair of which is now under way.

As to bridging, Exhibit 134 shows the linear feet of bridging, wooden, steel, concrete, or masonry, in two separate groups.

The bridging on the line from Denver to Dotsero via Pueblo is in good condition. Large proportion of it, the major proportion is of steel, masonry or concrete, or combination.

On the line between Denver and Orestod the major proportion of the bridging is wooden. There is at the present in for some renewals, a program has been made and is now being put into effect which requires the expenditure in the next three years to rebuild or repair the bridges between Dotsero and Denver and keep them safe for the motive power now operated over them, and that includes the Denver & Rio Grande Western power now used on that mileage. That expenditure will run about $30,920 in order to permit the Denver & Rio Grande Western currently to operate its very heaviest freight power, an additional expenditure of $10,400 will be necessary. And about three [fol. 1042] years hence, in a complete rebuilding program to bring all the bridging up to that standard and bring maintenance up to date, an additional expenditure of $27,300 will be necessary to rebuild outright some of the bridges, so that the money necessary to spend upon the Salt Lake Line between Denver and Orestod spread over the next three years to put the bridge condition in good shape is approximately $68,000.

By Mr. Clay:

Q. Mr. Hamilton, based on the exhibits before you, will the cut-off Moffat route be more costly to maintain in the future than the Tennessee Pass route?

A. No, sir, not in my opinion. I have just described its almost complete tie renewal, ties with 100-pound rail throughout. I am speaking now of the line between Orestod and Denver, the finishing of the ballast job, and a modest

expenditure of approximately $188,000 total for tunnel relining and bridge rebuilding, and when that is done the burden of maintenance will be very much lighter in the future. That speaks of the line between Denver and Orestod.

The line north of Orestod and——

Q. Well, just a moment. Have you any comment on the cross tie conditions of the Cutoff-Moffat route?

A. Yes, sir, the Cutoff line of the Denver & Salt Lake Western is a new railroad, the ties are three or four years [fol. 1043] old, and in good shape and adequate for the traffic. The tie renewals on the line between Orestod and Denver are being made thoroughly in connection with the laying of the new rail and the application of new ballast, and when that work has been completed, which will be sometime this year, tie repairs or maintenance of ties, such as there are, will largely disappear.

Q. At the end of the current year the charge will be very substantially diminished?

A. Yes, sir, very substantially, 50 per cent or more.

Q. What is your next exhibit?

A. An exhibit showing the profile of the line of the Denver & Salt Lake Railway between Orestod and Craig, the section of the line which is not operated over by the Denver & Rio Grande Western.

Mr. Clay: I would like to offer this exhibit for the record.

Examiner Boyden: Mark it Exhibit No. 162.

(Exhibit No. 162, Witness Hamilton, marked for identification.)

The Witness: In connection with that I have another exhibit, two sheets, entitled, "Physical Characteristics and Condition, May 1937", Orestod to Craig, Colorado.

Mr. Clay: I would like to offer that.

Examiner Boyden: Mark that 163.

[fol. 1044] (Exhibit No. 163, Witness Hamilton, marked for identification.)

Mr. Clay: Off the record.

(Discussion off the record.)

The Witness: As to Exhibit No. 163——

By Mr. Craig:

Q. Both of these exhibits pertain to the line from Orestod to Craig?

A. Yes, sir.

Exhibit No. 163, coupled with the profile, Exhibit No. 162, pretty thoroughly describe the line at its present physical condition.

Exhibit No. 163 is narrative in form and I think will speak for itself without any comment from me, except that it is the result of direct, first-hand observation.

I might say that the line is in good shape for the traffic it now carries; some modest improvement program, described in the exhibit, is in sight for the next few years, but nothing that need run up the current maintenance costs very much.

Q. Is this line from Orestod to Craig in good physical condition?

A. Yes, sir, it is in good physical condition for its present traffic volume and present operating needs. As to a very substantial amount of the track, the newly published time card speed restrictions are 60 miles an hour [fol. 1045] for passenger and 40 miles an hour for freight.

It does not need any extraordinary maintenance to hold it in satisfactory condition for future business. There are certain rail renewals as the exhibit states, required over the next six or seven years, but consistent and wise budgeting will carry that along without running up present maintenance costs.

The tie condition has been improved this year and the ballasting condition is being improved. The maintenance on that line need not run above 1935-1936, very probably will run below in the next year or so.

Q. How would you characterize the ballast conditions?

A. Sir?

Q. How would you characterize the ballast conditions?

A. It is sufficiently well ballasted, Mr. Clay, the character and quantity of the ballast are good. And if you wanted to sum up the whole situation I might say in just these words:

The ballast character and quantity and condition are good, the tie conditions are fair, they are improving; they are putting in a lot of ties right now. Tie plate protection

is good. The bridges are adequate for the motive power necessary for the economical operation of the line.

Now they have some scant banks, they are filling them [fol. 1046] as they clean the cuts. It is well-drained railroad. The rail condition, west of Steamboat Springs, the rail is being rebuilt by welding battered ends. The 63 miles east of Steamboat Springs requires some replacements. Consistent patching will enable the laying of new rail to be spread over several years, however, and the work which is now going on will be sufficient for some years to come.

Q. That is, the condition of this line is entirely adequate for passenger service demands?

A. It is.

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[fol. 1047] (Exhibit No. 209, Witness Paynter, received in evidence.)

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(Exhibit No. 210, Witness Paynter, received in evidence.)

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[fol. 1048] Examiner Boyden: Mr. Anderson, I stated this morning that the printed record of the court proceeding is complete in the Commission's docket up April 21, 1937, and it is understood that the printed record will be kept up to date. It is running about a month behind.

Mr. Anderson: Will that be considered as in the record for the purposes of this case?

Examiner Boyden: The Stipulation of counsel was that copies of papers sent to the Commission and filed in the docket constituted a part of the record before the Commission.

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[fol. 1049] MOTION TO STRIKE

Mr. Nicodemus: Mr. Examiner, may I have the right of way for a moment?

The R. & I. Trustee has circulated certain exhibits that are about to be introduced through this witness. One of them involves a document compiled under order of Division

4 in this proceeding in respect of which we wish to make a motion. I think perhaps it would be appropriate to make that motion now. The Debtor moves to strike from the files three documents: First, document entitled or denominated "Accounting investigation, Denver & Rio Grande Western Railroad Company" filed herein on or about July 29, 1936.

A corresponding study relating to the Denver & Salt Lake Railway Company admitted or filed herein on or about December 22, 1936.

Third, a report of the Bureau of Valuation filed under order of the Interstate Commerce Commission, or Division 4, entered on March 8, 1937.

These three documents were filed by order of the Commission, under Section 77-C(11) and the Debtor objects to the filing of these documents and moves to strike them from the record of this proceeding, on the ground that no hearing with the attendant right of cross-examination, or no [fol. 1050] notice of hearing has been had and that the data embodied in these several documents is not such as the Commission is authorized to file in this proceeding under Sub-section C, paragraph 11 of Section 77.

I make that motion at this time because we wish to object to the admission of certain of these impending exhibits on the ground that they are based on those studies.

Examiner Boyden: I understand that the witnesses of the Bureau of Valuation are available to the Debtor to examine in connection with any matters relating to the valuation report, and that witnesses will be presented, upon request, to testify relating to the accounting report.

You understand that, do you not?

Mr. Nicodemus: I did not understand it, but many of these studies have been filed after the proceedings were closed, not in this case, but in other cases.

Examiner Boyden: This proceeding is still going on. If you desire to call any witnesses, now is the time for you to do it, Mr. Nicodemus.

Mr. Anderson: Your Honor please, I have been somewhat embarrassed by these reports being filed in the record without any witness to testify as to the same, as to [fol. 1051] some of the provisions thereof, which I do not think would be admissible in any event, except in proceedings before this Commission, because the hearings here are less formal and they are in the nature of administrative

hearings, but when this record is certified to the court, our position becomes somewhat more difficult and if it went up on appeal from the court's decision, the question of this evidence might become quite vital.

I had not understood up to this time that we would be permitted to call the representatives of the Bureau of Accounts and the Bureau of Valuation as witnesses on these statements which have been filed by the Commission.

Examiner Boyden: Why shouldn't you?

Mr. Anderson: And I am not prepared this afternoon to examine those witnesses. I think I would like to reserve the right, if it is necessary, because I would like to go over those accounting questions and see if they affect our situation and if they are vital we would have to ask leave to cross-examine.

I do not know that they do. I do not want to prolong this proceeding nor do I want to take unnecessary steps and if it was only before this Commission, I would raise no question.

I would like to reserve consideration of that question, in view of the presiding Examiner's statement.

[fol. 1052] Examiner Boyden: Will you advise us as early as possible what you desire to do?

Mr. Anderson: I will take that up as soon as possible after this hearing is closed and advise you.

Examiner Boyden: Do you press your motion, Mr. Nicodemus?

Mr. Nicodemus: I submit the motion. I do not ask for a decision on it now; and I did not expect to get it, but I want to make a complete reservation of the right of cross-examining the witnesses of the Bureau of Valuation, or of the Bureau of Accounts, and to offer evidence in rebuttal.

Examiner Boyden: Of course, under the terms of the Act, those reports are prima facie evidence of the facts stated. There have been no witnesses presented for cross-examination, but if you desire to rebut the facts shown in there, the members of the Commission's staff who prepared those are available at your call to testify with respect thereto.

Mr. Nicodemus: One of the difficulties that we are laboring under is that it is difficult to separate the facts from the theories and the conclusions. We do not know what we are bound by.

Examiner Boyden: It would seem that that would be a matter that could be developed on examination of the witnesses.

. . . . . .

[fol. 1053] WITNESS JOSEPH R. WARNER

Q. Turning now to the investment base upon which to determine the rate of return, what do you find in the figures submitted by the Debtor?

A. I find that, except for the deduction of accrued depreciation on equipment, as shown on the carriers' books, it was based on the combined total of the investment in road, equipment and general expenditures, aggregating $210,539,779, less accrued depreciation on equipment, $8,955,785, or a net base of $201,583,994.

The figures I have cited are those as of December 31, [fol. 1054] 1934 balance sheet, or the middle of the test period.

Except for the amount of accrued depreciation, the results would not have been materially different from the corresponding figures at the beginning and end of the test period.

Q. Are these figures not correct?

A. They appear to check with those in the December 31, 1934 balance sheet included in the annual report to stockholders for that year.

Q. What is wrong with them?

A. The fact that although the Debtor used a realistic figure of depreciated book value in computing the 2 per cent rate of return on equipment, when undertaking to determine the rate of return on investment in road and equipment it adopted the artificial book values of the Debtor's balance sheet which are not realistic.

Q. Will you explain what you mean by realistic figures and artificial book values as you have used the term?

A. I mean that the depreciated book cost of equipment is usually more than a mere book figure, because in the first place it almost invariably initially represented the actual dollar cost of the equipment purchased, decreased by subsequent depreciation accruals.

Except possibly in the case of very old equipment, it follows strict accounting principles laid down by the Com-

[fol. 1055] mission, even though the carriers were allowed considerable latitude in the rate of depreciation applied. The substantial soundness of these depreciated book cost figures as a whole for equipment in the case of the Denver situation is evidenced by the fact that they tally closely with the reproduction new less depreciation figures filed in the record by the Bureau of Valuation.

Q. Is not this also true with respect to the book cost of road and equipment?

A. No, it is not, and the first prerequisite for determining the relative rate of return on different blocks of property is that the investment base or valuation be comparable.

This distinctly is not the case as regards the depreciated book cost of equipment used by the Debtor in computing the credits to the liens on equipment on the one hand, and the investment in road and equipment as a whole used by the Debtor for the purpose of demonstrating the low earning power of the property as a whole on the other.

Q. What would be comparable figures?

A. If we are going to use depreciated book cost figures for equipment which are substantially the same as the reproduction new less depreciation values compiled by the Bureau of Valuation, then we should use similar figures [fol. 1056] to determine the rate of earnings on the total investment in road and equipment.

Q. Where would you obtain these figures?

A. From the Bureau of Valuation's report to which reference has heretofore been made.

Q. Will you please do this?

Mr. Nicodemus: That is received subject to our motion to strike, which relates to that underlying data?

Examiner Boyden: Yes.

Mark the statement exhibit 246.

(Exhibit No. 246, Witness Warner, was marked for identification.)

Mr. Gammell: I submit that exhibit in the record formally.

Examiner Boyden: Any objection?

(No response.)

Received.

(Exhibit No. 246, Witness Warner, was received in evidence.)

A. The reproduction new less depreciation of road and equipment of the Denver & Rio Grande Western itself is given on page 3, sheet 1 of the Bureau of Valuation's report as $115,467,756, to which should be added for lands and rights, $5,428,159, or a total of $120,895,915, which is [fol. 1057] the item which appears in column 13 of the exhibit I have just submitted.

At the top of that column.

Similarly, the reproduction new less depreciation of the Denver & Salt Lake Western is cited at $3,880,723, plus $7,219 for lands and rights, which gives a total of $3,887,942, which appears in the second line of column 13 of the exhibit.

The comparable figures for the Junction are $3,409,074, plus $60,330 for lands and rights, or a total of $3,469,404.

The comparable figures for the Goshen Valley are $270,756 and $1908.

In each instance I have included non-carrier lands.

The grand aggregate of all these is $128,525,925. This figure is $73,058,069, or 36.2 per cent less than the Debtor's book cost figure of $201,583,994 for the Denver & Rio Grande Western alone.

In other words, the Debtor, for the purpose of demonstrating the low earning power of the property as a whole used an investment base which is more than 50 per cent higher than the reproduction new less depreciation plus land figures of the Bureau of Valuation, notwithstanding that the figures I have cited include the investment in both [fol. 1058] the Junction and the D. & S. L. properties which the Debtor's book costs does not.

It is apparent, therefore, that even if there be added to the Bureau of Valuation's figures, working capital which is stated at $2,473,400, an allowance for going concern and other elements of value, there would still be a very wide gulf between the inflated book values used by the Debtor for determining rate of return on investment and the more representative figures of the Bureau of Valuation.

Q. What was the relationship of the earnings from railway property which you have heretofore constructed from exhibits——

A. I might interrupt, if I may, to bring in something that is not in this exhibit.

Q. Very well.

A. In this exhibit, following down column 13, I have added in the $2,473,400 working capital. The Bureau of Valuation report arrives at a figure of $113,520,547.

There is not included in here the other elements of value which some might contend should properly be included in a computation of this kind. Ordinarily I would concede that to be unquestionably so. I am not sure that it is proper in this case, but if there be a difference of opinion on that, and there is latitude for such difference of opinion, I have ar- [fol. 1059] bitrarily added a figure of $5,895,805, at the bottom of column 13, and that is added in lieu of the cash working capital and gives a total of $116,942,959.

Now, that $5,895,803 is an arbitrary figure, but it is not picked out of thin air. It represents the excess in the Commission's valuation of the D. & R. G. W. properties as of June 30, 1919 and represents a difference in the D. & R. G. property between the values, between the Commission's finding of final value of $104,457,348 of the total owned property, including Junction, Kenilworth and helper railroads as of that date, and the $98,561,545 which is found as reproduction new less depreciation value, plus land as of that date.

Q. I was going to mention next the question of the relationship of the earnings from railway property which you have heretofore constructed from exhibits 107 and 113 to the aggregate of the Bureau's reproduction new less depreciation cost for the underlying properties.

A. A ratio of $2,713,082 to $128,525,925 would give a return of 2.11 per cent, or if you add the $2,473,400 of working capital, a return of 2.07 per cent.

Q. Are there any other factors you have in mind?

A. Yes; the very important one that we have two kinds of equipment and two kinds of railroad properties in this Denver situation. One is standard gauge and the other is [fol. 1060] narrow gauge and there is a wide difference between them, particularly as regards equipment. The Debtor itself indicated this when it cited on page 13 of exhibit 69 that there was no general market in which reproduction value could be quickly realized for narrow gauge equipment.

If the earning power of the railroad property as a whole is any criterion of a proper rate of earnings on equipment, we must obviously distinguish between the two entirely different kinds of railroad property and equipment and not confuse the results by commingling them.

Q. What adjustment do you suggest here?

A. A breakdown of both road and equipment values as between standard and narrow gauge.

Q. Can you do this?

A. I believe so, from the material at hand.

Q. Go ahead, please.

A. Take the figure of $2,713,082 as the earnings for the test period which consists of the net railway operating income, plus the potato adjustment, plus the ninety odd thousand dollars of net rents which it would appear were derived from property included in the investment base, and eliminate therefrom the narrow gauge results included therein.

[fol. 1061] As a matter of fact, the results of the operation of the standard gauge lines alone can be obtained from exhibit 70, 107 and 113. Taking the last mentioned, the earnings of the standard gauge lines can readily be constructed by adding the potato adjustment to the net railway operating income, which gives an adjusted net railway operating income of $3,328,307.

If we add to this the net of miscellaneous rents and the rents for leased roads, we obtain a figure of $3,402,233, as the earnings of the standard gauge lines in the test period, as shown by exhibit 103.

This figure, like the previous one constructed for the system as a whole does not include the outside income such as interest from the holdings of Salt Lake bonds, dividend adjustment on Utah Fuel Stock, etc.

I only mention that because the Debtor did include some of those things, but I want to make clear that I am not including the same outside items.

Q. How about the investment base?

A. As a rehearsal of the combination of these figures might be a little tedious, I have prepared herewith a schedule which I submit as exhibit 246, which shows the construction of the investment base; the computation of the narrow gauge valuation is shown in the bottom of this schedule, 246, which, deducted from the $128,525,925 gives a value

[fol. 1062] of $114,047,147. If we add the working capital to that it gives us $113,520,547, and with the adjustment for other elements of value in lieu of working capital would give a figure of $116,942,950.

Q. Had you finished with your explanatory part?

A. Yes.

Q. Did you want to say anything about the rate of return?

A. The relationship between the $3,266,892, which is income from railway operations shown in this exhibit 246 for standard gauge lines only, to the investment base in standard gauge lines, gives a relationship of 2.94 per cent. That is the relationship of the income from the standard gauge lines to the reproduction new less depreciation element of value assigned to those lines, exclusive of so-called other elements of value, but including the land.

Mr. Hoffman: And including equipment.

By Mr. Gammell:

Q. The investment figures from which you construct this——

Mr. Hoffman: But including the depreciated value of equipment, Mr. Warner?

A. How?

Mr. Hoffman: But including in that figure the depreciated value of equipment?

[fol. 1063] A. Yes, the depreciated value of equipment is in it, these figures embrace both the property and the equipment, reproduction new less depreciation.

Examiner Boyden: All right.

By Mr. Gammell:

Q. The investment figures from which you construct this 2.94 per cent are merely the sum of the elements of value for the standard gauge lines as found by the Bureau of Valuation as of December 31, 1935, and do not embrace the going concern and other values, if any, which might attach to the property.

A. Well, I have substantially covered that before in the discussion, because I put in a computation of this kind. The other elements of value are properly includable, but

as there is latitude for diversity of opinion on that score, I have shown those figures here, if one wants to include them, they make very little difference, however, if this point be waived and the elements of value be stepped up by the amount which the Commission's finding of final values for the Denver & Rio Grande Western properties exceeded its then reproduction less depreciation values, or $5,895,893, would bring the total investment base up to $116,942,950, to which the income of $3,266,892 would bear a relation of 2.79.

I am not, however, conceding that if a return on equipment is to be any way influenced by the return on the prop- [fol. 1064] erty as a whole, the value of the latter adopted for such purpose should be more than the comparable figure for equipment, that is, bare elements of value, or specifically, in this instance, reproduction new less depreciation. And as this exhibit shows, the return on reproduction less depreciation was 2.94.

[fol. 1065] E. H. Burdick was sworn and testified as follows:

Direct examination.

By Mr. Fitzgibbon:

Q. Mr. Burdick, you have been retained by the Guaranty [fol. 1066] Trust Company of New York in this matter?

A. I have.

Q. What were you asked to do?

A. I was asked to value the stock, the common stock of the Utah Fuel Company on a going concern basis.

Q. What was your engineering education, Mr. Burdick?

A. I spent three years at the Colorado School of Mines, not finishing the course for financial reasons at that time.

At several times afterwards and during the last fifteen or eighteen years I have done advance work at the University of Utah, specializing in geology, and during those times of attendance lecturing in the economic geology class on coals.

Q. What has been your professional experience in the industry?

A. From 1904 to 1906 I was chief engineer of the Great Western Fuel Company operating in Fremont County, Colorado. From 1906 to 1917 I was in independent practice, with my office at Durango, Colorado.

During this period of practice at Durango I had occasion to examine many coal mines and properties. During that time I examined and valued properties, undeveloped properties largely, owned by the Union Pacific Railroad through [fol. 1067] their subsidiary company, the Porter Fuel Company.

Q. Have you had any connection with the Utah Fuel Company and its affiliate?

A. Yes, sir. During the entire period from 1906 to 1917 I was retained at various times to do work for the Calument Fuel Company, a subsidiary of the Utah Fuel Company. In 1917 I had my first salaried connection with the Utah Fuel Company. My duties were as technical advisor, mining engineer, for the operations, particularly in Colorado.

In 1919 I was transferred to the general offices in Salt Lake City and still carrying no specific official title. My duties were as assistant to the president and in technical charge of the operations of the company in Colorado.

This connection lasted until 1922, since which date I have been in independent practice in Salt Lake City, specializing in fuels.

During the time in Salt Lake City from 1923 to date I have been the Geologist for the State Land Department, having charge of the leasing of mineral lands, and for a five-year period, from 1927 to 1932, I was consulting geologist for the Tax Commission of Utah, valuing the non-metallic minerals and particularly coal mines for the purpose of taxation.

[fol. 1068] I might explain here that the tax structure in Utah on coal mines is more or less an exact structure. The recoverable reserves in each given tract are calculated after rather close examination and certain values assigned according to rule.

Since 1933 I have been acting State Geologist for the state.

Q. And in connection with that have you valued for sale purposes other mining properties?

A. In connection with my private practice, yes, sir. I might state that the state of Utah is simply a client of

mine, not a salaried connection. During that period I valued for sale purposes mines aggregating probably 30 or 35 per cent of the coal tonnage produced in Utah.

Q. Will you give a brief statement of the geological situation in Utah and Colorado?

A. The coals of the Rocky Mountain field, including those in Colorado and Utah, occur in the lower parts of the upper portion of the cretaceous horizon. I speak of this particularly to distinguish them from the coals of the Appalachian region, which are in the Pennsylvania main, which are very much lower.

This fact has a considerable bearing on the operations of the various coal mines. The coal beds are relatively flat lying, and therefore are opened by tunnels from the [fol. 1069] outcrop. There is only one operating shaft mine in the state of Utah.

Mr. Fitzgibbon: There is nothing in the report in regard to this; I do not know how far the Examiners wish to go in connection with it.

Examiner Boyden: Well, only as far as is necessary to support your report.

Mr. Fitzgibbon: Well, it is sufficient for my purposes.

The Witness: I might state here that in discussing the values of the Utah Fuel I am considering the Consolidated Fuels and the acreages of the Utah Fuel and the present Valley Coal Company.

They used to be distinct companies although the same general operation, but a few years ago the charter of the present Valley Coal Company expired by limitation and the Utah Fuel holds all the properties of the present Valley Coal Company, so as far as this report is concerned the values are based on the original Utah Fuel, plus the present Valley Coal Company and the Calumet Fuel Company and various other smaller subsidiary companies.

By Mr. Fitzgibbon:

Q. Since 1922, have you from time to time been retained by the Utah Fuel Company for their particular problems? [fol. 1070] A. I have.

Q. Have you recently made an examination of those properties?

A. Yes, sir, I made a rather detailed examination of the coal properties in Colorado. I have been very familiar

with the operations in Utah, my connection with the Utah Tax Commission requiring that I go through these properties at least once a year.

Q. Where have you gotten all of the statistical information included in this report?

A. As far as the sheets that refer to accounting, they are obtained from the auditing department of the Utah Fuel Company and were furnished at my request in order that I might gain sufficient basic data on which to fix my valuations.

Q. Have you examined or had submitted to you various exhibits which have been offered in this case with relation to the Utah Fuel Company?

A. I have.

Q. Do you know that it was not many years ago when the equity in this stock, half of it, was valued at many millions of dollars?

A. That is my information, yes, sir.

Q. You know that these bound sheets carry the properties so far as the stock is concerned at from ten to fifteen [fol. 1071] million dollars?

A. I do.

Q. How is it then that you reach in this report a valuation of slightly less than five million dollars?

A. In order to answer that question one would have to outline the history of the coal industry in Utah so far as it affects the Utah Fuel Company.

Or possibly it would be more properly stated to say an examination of the history of the Utah Fuel Company in two sections:

First, from the time of its formation up to 1921, and the changes that have occurred from 1921 down to the present date.

The explanation of the first part of their history has a direct connection with the geology of coal mines in Utah. As I said before, the coal beds are flat lying, but instead of being one seam there are a series placed in parallel position, one above the other.

Prior to 1908 the only mines, railroad mines, operating in Utah were the property which is known now as the Sunnyside Mine, the Castle Gate Mine, Winter Quarters Mine and the Creek Mine. The general conception was that

there was simply one coal bed throughout this field, known as the Castle Gate coal bed.

About 1908 it was discovered that there were beds above, [fol. 1072] and commencing about 1913 there began a period of intense development of these coal seams. Up until that time the Utah Fuel Company enjoyed a practical monopoly on the coal business in Utah. From 1912 to around 1920 or 1921 there were some sixteen large coal mines, or fairly large coal mines opened.

This, of course, made severe competition, particularly so as the market for Utah coal is a very restricted market.

Q. Where is it principally sold?

A. The state of Utah, Idaho, to a limited extent Nevada; in the early days California was a very fine market. Oil was discovered in large quantities and became a serious competing factor after 1921. Up to 1921 the largest mine by long odds that the Utah Fuel Company owned was the Sunnyside mine, and in connection with this mine there were some 800 small beehive coke ovens operated. This was a very profitable business.

The Somerset Mine, in western Colorado, one of the properties of the Utah Fuel Company, was operating at maximum capacity. So that by 1921 we had the Somerset Mine, the Sunnyside Mine, Castle Gate No. 4 Mine, and a second mine at Castle Gate which was opened prior to 1921, known as Castle Gate No. 2 Mine; the Winter Quarters Mine, a mine producing at that time some 400,000 tons a year or better, and the Clear Creek Mine.

[fol. 1073] All of these properties were operating at practically maximum capacity as of 1921.

Now, taking up the period from 1921 to the present date. The first explosion at Castle Gate No. 2 Mine occurred. This was in March 1924, a very disastrous explosion which wrecked the mine very badly and there was a terrific loss of life. In August 1928, the second explosion occurred and while there was no loss of life the property damage was very large.

The main standby of the company at Castle Gate was the Castle Gate No. 1 Mine which had a superior grade of coal; and in November 1929 this mine caught fire and was sealed and so remains to the present day.

In 1928 the Winter Quarters Mine was abandoned, the town dismantled, buildings sold, and today it is rather

difficult to tell where the Winter Quarters Mine was located.

I neglected to state, in the period prior to 1921 another small mine, known as the Utah Mine—it was not of great importance, its maximum production reaching possibly 50,000 tons a year. In 1925 the Utah Mine was abandoned, the buildings removed, the portal of the mine is now caved in.

The most serious loss subsequent to 1921 was the loss of the coke trade at Sunnyside. I might state that the [fol. 1074] Sunnyside Mine and a few thousand acres adjoining it on the South constitute the only coking coal in the state of Utah.

The Columbia Steel Company had come into the state and had built some iron furnaces at Ironton, near Provo, and acquired the ground south of Sunnyside.

They constructed by-product coke ovens, and thereby were able to underbid the Utah Fuel in their coke business. As a consequence the Utah Fuel lost this business, the Sunnyside Mine which had previously produced from, say, 400,000 tons, and in one year I believe as high as 800,000 tons, was largely closed down and a share of the houses sold, and today this mine is producing only about 50,000 tons.

The product cannot compete in the somestic market on account of its being a heavy coker.

Q. A heavy what?

A. A heavy coker.

Examiner Boyden: What do you mean by "heavy coker"?

The Witness: Well, the coals of Utah are non-coking. That is, when they burn they burn simply to an ash. You cannot make metallurgical coke except at the Sunnyside Mine and the Columbia Mine, the products of those two coals.

You use either of those coals in a stove and it simply [fol. 1075] cokes into a hard mass.

Now, during this period the Utah Fuel——

Examiner Boyden: Excuse me just a minute, now. Does that make that coal advantageous or disadvantageous for ordinary fuel consumption?

The Witness: Disadvantageous.

Examiner Boyden: Does it make it advantageous for coking purposes?

The Witness: Oh, yes, it makes a very fine metallurgical coke, that is used in the smelters and the blast furnaces at Ironton.

Examiner Boyden: That is the Sunnyside Coal you are talking about?

The Witness: That is the Sunnyside Coal, and when they lost their coke contract they could no longer operate the Sunnyside Mine, that is, to operate it to anywhere near capacity.

By Examiner Boyden:

Q. That is, they were unable to compete with the new producer in spite of the fact that they produced a good coking coal?

A. Yes, sir; the Columbia has the same coal, it practically adjoins Sunnyside.

By Mr. Fitzgibbon:

Q. Are there any particular operating advantages that one mine has against the other?

A. No, as a matter of fact I think probably the Columbia [fol. 1076] has the advantage. If you wish me to state the reason, I can.

Mr. Fitzgibbon: Well, I think we can take his conclusion.

Examiner Boyden: Very well.

The Witness: During this period the company opened one mine, it is a small shaft mine, located at Castle Gate, and is known as the Castle Gate No. 3 Mine. This mine operates a coal bed probably 250 feet vertically above the Castle Gate seam. The coal is all right for domestic purposes, but cannot be sold for stoker purposes because the fusion point of the ash is too low.

So when we come to the present date, the only mines of the Utah Fuel operating are the Somerset Mine in Colorado, which is a good mine.

Q. What about the quality of the coal?

A. That is a very good quality of coal. It is non-coking; it won't make metallurgical coke but it is a very nice quality of coal as western coals go. The Sunnyside Mine is operating at around 10 per cent of maximum capacity; the Castle Gate Mine and the Castle Gate No. 3 Mine at Castle Gate, and the Clear Creek Mine operate at 50 or 60 per cent of capacity. The reason for, the main reason for the re-

stricted capacity at the Clear Creek Mine is that the ground [fol. 1077] is nearing exhaustion and the workings are thin and in other words filled with broken stone, destroying the value of the coal very largely in thos- broken stones.

This coal is really only good for domestic purposes, as it will not keep while in storage, it has too high a moisture crystallization, it breaks down badly on exposure to the air.

Q. What is the proper amount of air in that field to maintain the keeping qualities of the coal?

A. I have given the analysis in here. A 3 per cent moisture crystallization coal, as far as Utah is concerned, is a very good coal. As soon as you get above 5 per cent moisture you can look for the coal to break down upon storage.

Another factor that might be mentioned in here is that all Utah coals fire on storage. This is particularly true of slag piles.

I neglected to state, regarding the Somerset Mine, which is located in the same coal horizon as the Castle Gate Mines, the workings go under terrific cover. I mean by "under terrific cover" that in following the down dip of the flat lying coal bed, that is, flat along its strike and dip, approximately 5 degrees away from its outcrop you get increasingly deeper into the ground.

In addition to that the mountain ranges rise from the [fol. 1078] outcrop. Under this heavy cover spontaneous fires commence to generate and the large Somerset seam, which was about 13 feet thick, had to be abandoned, and operations transferred to a coal bed 50 feet higher, which runs from 6 to 8 feet.

Examiner Boyden: When you say that the Utah coal fires in storage, you mean that it will take fire from spontaneous combustion?

The Witness: Yes, sir.

By Mr. Fitzgibbon:

Q. That is, while it is in the ground?

A. Well, in the case of Somerset, yes, but I think you were referring to after it is mined and piled up in the yards.

Examiner Boyden: Yes.

The Witness: It fires very readily when it is in storage, Mr. Examiner.

Stated briefly, the shrinkage in output and of potential output accounts for the differences between the high values of a few years ago, which quite possibly were entirely justified, and the valuation which I have placed upon this property in this report.

By Mr. Fitzgibbon:

Q. Have you any other remarks to make as to the quality of the coal now being mined, other than what is in your [fol. 1079] report, or do you think that that covers it sufficiently?

A. Well, I think that covers it sufficiently but I would be very glad to go further into that, if you care.

Examiner Boyden: I think it is sufficient, if it is sufficient to form a basis for your report; make your report understandable.

By Mr. Fitzgibbon:

Q. Are you familiar with current wages and costs of supplies in Utah and Colorado?

A. Yes sir, I am quite familiar with wages, and, in a general way, with the cost of supplies.

Q. And current coal prices?

A. Yes, sir. I might say here that in—I will explain what my summation will show by making some explanation regarding the Calument Fuel Company if you want me to do it at this time.

Mr. Fitzgibbon: Off the record.

(Discussion off the record.)

By Mr. Fitzgibbon:

Q. Oh, yes, if you would take up the Calument at this time, please.

A. The Calument Fuel Company has——

Q. This is on Colorado, now?

A. Yes, sir. On page 19 of the report the joint set-up of the Calument Fuel Company is stated, the physical set-up.

Commissioner Meyer: Are you going to offer the re- [fol. 1080] port?

Mr. Fitzgibbon: I am. Do you want me to offer it now?

Commissioner Meyer: Let's give it an index number or exhibit number. We will mark it Exhibit 253.

(Exhibit No. 253, Witness Burdick, received in evidence.)

The Witness: As of 1921, the Calumet Fuel Company was operating one mine in Colorado. And all of their operations have always been in Colorado. This was known as the Perins Peak Mine and was located some three or four miles northwest of Durango on a branch, which they owned, by the way, some two or three miles long, connecting with the narrow gauge Rio Grande Southern Railway.

The Perins Peak Mine is one of the mines that was completely worked out before anything happened to it. The Calumet Company—it was worked out in the middle, possibly about 1925 I believe the work there was abandoned. It is set forth in the report, the exact date.

In Huerfano County, Colorado, the Calumet Fuel Company owned a tract of coal ground, just north of Walsenburg comprising close to 4000 acres. There were three mines operating in this tract, under lease. What was known as the Turner Mine, the Gordon Mine and the Vesta Mine. The Calumet No. 1 Mine was on the larger coal bed. There [fol. 1081] are two seams of importance in that territory, the lower one known as the Cameron bed and the other one the Walsenburg bed.

The seams or coal beds, I am using those terms synonymously, are very much smaller in the Walsenburg district. The Cameron coal bed runs from 36 or 40 inches up to, in some cases, 5 feet, 5½ feet.

The Walsenburg bed is a larger seam, running generally 7 or 8 feet in this particular district.

The Utah Fuel Company, or the Calumet Fuel Company, took over the Turner Mine and operated it as a company operation until December 1933. The various mining troubles developed and in part of the territory the coal bed became much thinner and dirty, and they had to close the operation and transferred their activities to a mine adjoining on the south, within their land, which is now known as Calumet No. 2 Mine.

The Calumet No. 2 Mine is on the Cameron seam and produces a very nice grade of coal, particularly for domestic use. The original Turner Mine, or Calumet No. 1 Mine produced a coal that was considered not a very good keeper but was pretty fair for locomotive use, and they had a substantial railroad contract. The normal output of the Calumet No. 2 Mine at the present time is 75,000 or 80,000 tons

[fol. 1082] a year, and I believe will reach 100,000 tons or more a year for the period until the coal reserves are exhausted.

By Mr. Fitzgibbon:

Q. You refer in the report to the turning back of certain of these coal lands to the state in order to avoid taxes, not to avoid taxes, but to give back the land and therefore relieve the corporation of tax burdens, do you not?

A. Yes, sir.

Q. How long ago was that done?

A. It has been done in succeeding years, commencing about 1931 or 1932. Did you wish me to go into that?

Q. I want you to state your opinion as to whether or not that was done wisely or not, and state the basis of the advantage.

A. I think that it was very wisely done.

Q. And why do you say that?

A. In the first place, when these lands were acquired, Utah had such a taxing system that a very negligible burden was placed on an operating company on account of its bad reserves, that is, the coal that was not being operated. It was on this theory that the Utah Fuel Company acquired these lands. Commencing in 1917 the system of taxation was changed, as I have explained, it was based on the tons of coal in reserve.

The lands largely that were surrendered were backlying [fol. 1083] lands and if we think again of your geography of your mountain chains piling up back from the outcrop, they were nearly all under very heavy cover. That is, there was a terrific pressure on the coal. They were not "get-at-able" except from the outcrop, the shaft operation generally speaking would be way too deep. No one else could operate these lands and as a matter of fact using any reasonable forecast as to tonnage production the coal reserves would not be necessary for some hundred or hundred and fifty years, in fact, there is some of that backlying land that would have been longer than that.

The tax burden with the drop in tonnage was becoming prohibitive. The assessed taxes per ton of the Utah Fuel Company eventually amounted to some 26 or 27 cents for every ton *out* output, which really removed the chance of any profit, and hence these lands were surrendered.

Now, the taxing system on non-operated coal lands in Utah is based on substantially when you are going to get to them. They are called A lands, B, C, and so forth, the A lands being a subdivision in which are mine workings, and those are valued for taxation purposes at 4 cents per ton. The lands adjoining and within one mile of an operating mine are classed as B lands, and are given a value of 2½ [fol. 1084] cents per ton. The land adjoining the B lands are classed as C, and are given a value of ½ cent per ton.

Now, up to this point experience has proven that the tax structure in Utah results in a value that closely approximates the actual value.

Now, when you go into these lower classes, D, E, F, and so on, they impose a tax burden that is inordinate and if you add the value of those lands to the A, B, and C lands you have got a resultant value that is considerably more than the actual.

The abandonment of some of the lands was brought about by the fact that the operation which normally should develop those lands had been abandoned. This automatically reduced the assessed valuation to a lower class.

I might say that in assessed valuation of coal lands, they do not value the gross tonnage; they proceed on the theory that 60 per cent of the gross coal is mineable.

Examiner Boyden: Mineable?

The Witness: Mineable. That is, they can produce 60 per cent.

Experience is not bearing that out under the heavy cover lands, that is, those that have a heavy burden over the coal.

By Mr. Fitzgibbon:

Q. Am I correct in interpreting your testimony and re- [fol. 1085] port so as to mean that in the surrendering of those lands nothing was lost but something was gained?

A. I think there was a great deal gained.

Q. And the coal lands were really, insofar as the Utah Fuel Company was concerned, they were not given to someone else with the power to take the coal out?

A. No, sir.

Q. Is there anything you want to say before proceeding to the elements as to valuation?

A. I think not. I think that is covered, at least in the outline in the report.

Q. Well, what has been your approach to the valuing of the property?

A. I considered, insofar as the Utah Fuel is concerned, the earnings in the past, and have endeavored to forecast a reasonable earning in the future. This takes into consideration, of course, the general conditions, the loss of the coke business, and so forth.

I have also considered the income statements and the balance sheets of these other companies, and from all of this I have arrived at this conclusion; that an average of the new money earned in the period including 1929 to the present date is a fair average of what can be expected in the future life of the property under a certain set of conditions which we are taking as basic.

[fol. 1086] In the first place, in fixing a valuation we will have to consider the reasonable depreciation based on the new tonnage which we are calculating is going to be produced on an average in the next 40 year period.

The tonnage reserves I think can be passed with the statement that they are more than ample to supply a mine producing the tonnage I have estimated for the 40 year period. As a matter of fact, the reserves would be ample to supply this mine for probably a 70-year period.

Q. Why is it you base your calculations on a 40-year period?

A. Well, 40 years is about as far as I want to go in fixing a valuation.

From these reports, which are all included in the statement, the income statement, and so forth, in this report, the latter portion thereof, marked "addenda" I conclude that a fair new money expenditure would be 33.8 cents per ton; that a reasonable depletion allowance would be 12 cents a ton, and to return the value of it I have placed a depletion allowance of 3 cents a ton.

The next question is to determine what will the output be.

Q. Before you leave that, for a moment, why was it that you took the years 1929 to 1936?

[fol. 1087] A. The coke contract was lost prior to 1929 and in my judgment this coke business can never be regained. A large part of the earnings in an early day were from the Sunnyside operation and I have to delete from my basic data those periods in which the Sunnyside Mine was operating. Is that sufficient?

Q. Yes, that answers my question. Thank you.

A. The next question is to determine how many tons of coal are you going to produce. An examination of the history of the years taken as indicative for value, the Utah Fuel Company has produced in Utah about 20 per cent, which has been an increasing amount.

Q. Is that shown on page 24 of your report?

A. Yes, sir.

Q. In chart form?

A. Yes, sir, it is shown in chart form, and also the complete tabulation, including Somerset, appear at other points in the report.

Q. I did not mean to interrupt you.

A. That is perfectly all right.

Q. I just wanted to make it easier for people to follow.

A. Applying this figure of 20 per cent to the total Utah production, less the coking coal production, gives in my judgment an average expectancy during the next 40 years of 1,200,000 tons per year. In other words, the production [fol. 1088] of the State of Utah will increase sufficiently so that 20 per cent of this production will amount to 1,200,000 tons per year. To this total must be added a reasonable tonnage for the Somerset Mine which I have placed at 720,000 tons per year, making a total expectancy of production of the 40-year period of 56,800,000 tons which, at 14.7 cents per ton, indicates a net profit of $8,349,600, or a return of $208,740 per year.

Now, it must be borne in mind that this return is based on what the land will produce with the aid of the plant on the ground. So this resultant value which comes on the basis of ascribing a 6 per cent return on the money, a value of land and plant, present day value of land and plant, of $3,479,000.

From this must be subtracted the value of the improvements and equipment to give the value of the coal lands. This amount of equipment and improvements is depreciable, which will be later discussed, comes to $1,641,460, giving a value for the coal lands of $1,837,540. I have assumed more to give recognition to the residual land after this 40-year operation, an arbitrary figure of $50,000 which added gives a total value of the coal lands of the Utah Fuel Company of $1,887,540.

Q. Now, how did you value the Calumet Coal Land, by the same method?

[fol. 1089] A. No, sir. The operating history of the Calument No. 2 Mine is not of sufficient length to give a yardstick, as to earning capacity. I have assigned a lump value per ton of coal equal to the going royalty in that district, which is 10 cents per ton. And discounting that royalty to get present day value.

Multiplying this by the tons of recoverable coal will give the present day value of the coal lands.

In the case of the Calumet Fuel Company the non-recoverable tonnages have shrunk very materially as the workings went into the tract owned by the Calumet Company and as drill holes were sunk it was found that there was not nearly the amount of recoverable coal that was estimated in the first place. The recoverable coal reserves in the tract owned by the Calumet Fuel Company are now quite definitely placed at 2,000,000 tons. Assuming an annual mine production of 100,000 tons, would give a life of the mine of 20 years.

The present value of the 2,000,000 tons of coal on the 10-cent royalty basis, 20 years at 6 per cent, gives a total present value of coal lands of $114,698.

Now, in this case the value is for the lands alone. In other words you might say rental of these coal lands. To this should be added in this case the additional value of plant and equipment.

[fol. 1090] Q. Why should that be added, in the other case you deducted it, did you not?

A. Because that was based on the use of both land and plant. In this case on a royalty basis the value is based on the use of the land alone, therefore we should add the value of the plant.

Q. You mean that if they were leased at this royalty the lease would not include the equipment and other property that would be there?

A. No, sir, it is simply rent on the land, to state it in other terms.

Adding this value of plant and equipment, which amounts to $172,385, gives a total value of the Calumet Fuel Company of $287,043.

The sum of the Utah Fuel Company valuation proper and the Calumet Fuel Company would then be the value of the physical coal properties.

Q. Are you conclusions as to value set forth on page 33, that is, page 33 of Exhibit 253?

A. Yes, sir, they are.

But these conclusions of value are based on considerably more data than just for the two companies. In other words, there are certain subsidiary companies, other small companies, and the summation of value was based on the value of the physical property and the balance sheets of the small [fol. 1091] subsidiary companies. That is set forth in the consolidated statement of values on page 35, which is again repeated on page 34.

This in total shows a value for the Utah Fuel Company and its subsidiaries of $4,653,720.30 as tabulated.

Q. You mentioned page 35 a few seconds ago; you meant page 33?

A. It is set forth on page 33 and repeated on page 34.

Q. Have you tried to check this valuation against other methods?

A. I have.

Q. What has been—tell us what they are.

A. Since this report was submitted, in fact, since I came to Washington I endeavored to check my totals by other methods of valuation.

First, on a royalty basis, the same as in the case of the Calumet Fuel Company. In Utah the going royalty, both of government and state leases, is 10 cents a ton. Applying the factor of ultimate 10 cents a ton royalty to present day value at 6 per cent, and applying that to 56,800,000 tons, that gives a value for the coal lands of $2,186,476. To this should be added to make it comparable, the $50,000 residual value, making a total value of $2,236,476. To this should be added the same value for depreciables as I used in my origi- [fol. 1092] nal valuation, giving a value for the physical property and equipment of the Utah Fuel Company of $3,287,936, as compared to the $3,529,000 shown in my report.

Q. Now, those items, $3,529,000, are approximately the totals of items 1 to 4 on page 33?

A. Yes, sir.

A second check was the assessed value. And taking the assessed value of the Utah Coal Lands, which amounts to $1,603,605.

Colorado has no exact rule of valuing coal lands. The Somerset unit, that is, those lands in which the coal is tributary to the Somerset operation, is assessed at $80,000. I think this is unquestionably low. This gives a value of

For purposes of depreciation, the Internal Revenue Department years ago fixed a basic value for the Utah Fuel Company and the Calumet Fuel Company of $5,594,923.36, less the allowed depreciation to date amounting to $1,312,026.60, leaving a remaining value of $4,282,896.76, which would be comparable to the land and depreciables of the Utah and the Calumet Fuel Company, which appear in that report.

I might say in this connection that within the last two weeks, the department of Internal Revenue has okayed the depreciation figure for 1935 and 1936 on this basis of valuation.

By Mr. Fitzgibbon:

Q. About the administration of these properties, both executive and from the operating point of view, have you any views on that?

A. Yes, sir; I am well acquainted with the operation of the coal properties in Utah and production costs, and so forth.

[fol. 1095] Examiner Boyden: Suppose we postpone that until two o'clock.

Mr. Fitzgibbon: Very well.

Examiner Boyden: We will recess until two o'clock.

(Whereupon, at 12:30 o'clock, p.m., a recess was taken until 2 o'clock, p. m., of the same day.)

[fol. 1096] AFTERNOON SESSION

The hearing was resumed at 2:00 o'clock p. m.

Examiner Boyden: Proceed, Mr. Fitzgibbon.

E. H. BURDICK testified further as follows:

Direct examination (Concluded).

By Mr. Fitzgibbon:

Q. Mr. Burdick, how does the organization of the Utah Fuel Company and its affiliates compare with the others in the field; by "field" I mean Utah and Colorado?

$1,683,000 plus. To this should be added the $50,000 residual value, giving a value for the coal land on the assessed value basis of $1,733,605, and which would be comparable with the $1,887,540, used in my report.

If we are going to carry the thought of assessed value through in this comparison, to the assessed value of the coal lands should be added the assessed value of the depreciables, amounting to $903,970. The assessed value of the depreciables is low. The items that they get, such as buildings, houses, the visible items, you might say, are assessed at full value or more, as far as Utah is con- [fol. 1093] cerned.

However, using this assessed value of $903,970, gives a total of $2,637,000, odd. This compares with the $3,529,000, as shown in items 1 to 4, is that right?

Q. Yes, on page 33 of the exhibit.

A. I used as a third check, taking the assessed value of lands and adding to that amount the adjusted value of depreciables used in my report. The same amounts to $3,375,065, which compares with $3,529,000 in the report.

As a fourth check——

Mr. Fitzgibbon: Off the record a moment.

(Discussion off the record.)

By Mr. Fitzgibbon:

Q. Mr. Burdick, when referring to items 1 to 4 as being comparable, did you mean with the figure of $2,637,000, was I correct?

A. No, sir, because that included the value of the surface lands held by the Utah Grazing Lands Company, a subsidiary company. That is more properly expressed as Items 1, 2, 4 and 5. It compares with the value of the lands of the Utah Fuel Company, the lands of the Calumet Fuel Company, the depreciable property of the Utah Fuel Company and the depreciable value of the Calumet Fuel Company.

Q. What figure is that in your testimony that those items [fol. 1094] compare with?

A. Those four items compare with my—those totals that I have given compare with the sum total of items Nos. 1 to 4. That is the coal lands of Utah Fuel and the depreciables.

Now, the totals that I am going to give you now compare with items 1 to 4 and 5.

A. It is among the most efficient.

Q. And does that cover the executive and operating?

A. It does; the company has an exceptionally strong morale and I might say that the Utah Fuel is in the low cost group. Their costs will run probably 25 cents a ton under the field average.

Examiner Boyden: Will you read the answer?

(Answer read.)

By Mr. Fitzgibbon:

Q. Well now, do you tie those two together, I was just asking about the operation personnel and the executive personnel?

A. I tie the two together.

Q. Well, is there anything in the property that has something to do with the fact that they are in the low cost group? [fol. 1097] A. Yes, sir; in a general way I would say in some of the properties they have remarkable mining conditions; in others not so favorable.

Their low costs I think are primarily due to efficiency in management and operations.

Q. It has been suggested from time to time that these coal mines were very dependent upon the railroad serving them; have you any comment to make in regard to that?

A. I think that that is true, but on the other hand the railroads are very dependent upon the coal mines, they furnish them a large, a very considerable tonnage.

Q. On page 107 of your report you had a correction to make in that?

A. Yes, sir.

On page 107, in the fourth column from the right hand, the heading "Tonnage" the totals shown there are pointed off wrong. There should be a decimal point between the second and third figure from the right.

Q. To illustrate?

A. To illustrate, the first entry should read 10,531.75 tons.

Q. Can you tell us something about this slack coal?

[fol. 1098] Examiner Boyden: That should be all the way down the column?

A. The Witness: That should be all the way down the column, yes, sir.

By Mr. Fitszgibbon:

Q. Can you tell us something about this slack coal, what is slack coal, very briefly?

A. Slack coal is the nut size or what will go through whatever is adopted as the minimum screen aperture, it may be one inch or it may be 1-5ths inches.

Q. How does this coal compare with the oversize coal for the purpose of the railroad operation?

A. Well, it is just as good, and it is best adapted for use in automatic burning equipment; stoker.

Q. Just as good, no better no worse?

A. Well, you can't burn the large sizes in the stoker equipment so the coal has to be nut size for the stokers on locomotives.

Mr. Fitzgibbon: Off the record.

(Discussion off the record.)

By Mr. Fitzgibbon:

Q. Have you another correction on page 13?

A. I have; near the top of the pag item numbered 3, there should be added "Castle Gate No. 3 Mine". I speak of it as being opened at the top of the page, but do not [fol. 1099] include it in the summary, so line 3, shall read "Castle Gate No. 2 mine and Castle No. 3 Mine."

Mr. Fitzgibbon: That is all.

Examiner Boyden: Any cross-examination?

Mr. Hoffman: May I ask one question, please?

Examiner Boyden: Mr. Hoffman.

Cross-examination.

By Mr. Hoffman:

Q. In fixing approximately $5,000,000 for the going concern value of the Utah Fuel and its subsidiary companies, have you given any added weight to the fact that the depreciation and depletion are so to speak free of taxes?

A. No, sir.

Q. Now, in respect of those properties, you have valued on the so-called royalty basis, have you given any added value or consideration to the fact that a concern owning

those properties has customers, may have been established for some considerable time and may have what we more or less denominate as a going concern value?

A. I have given no value to such items as such, but in fixing the return of 6 per cent I recognize the fact that they are going concerns. With a new concern or a new operation you would probably capitalize on the basis of 8 or possibly 10 per cent.

[fol. 1100] By Examiner Kirby:

Q. Mr. Burdick, in valuing the Somerset property or the property of the Utah Fuel Company, which is summarized on page 26 of your Exhibit, have you in effect projected over a period of forty years an average net income per ton of 33.7 cents?

A. No, that is——

Q. Less the deductions, of course.

A. Less the deductions, yes, sir.

I assumed new money of 33.7 cents.

Q. That is after cost of operation, isn't it?

A. Yes, sir.

Q. Have you assumed that the cost of operation over that entire 40 year period would remain constant?

A. No, sir, the best that we can do is to deal with averages and judging the future by the experience of the past, modified by the conditions as we know them as of today.

In effect though it is a constant of 14.7 cents, or new money of 33.7 cents.

Q. Well, the 33.7 cents is the average net income per ton, isn't it?

A. Before depreciation and depletion.

Q. And after operating expenses?

A. Yes, sir.

[fol. 1101] Q. At the end of 40 years you will be approaching the point of exhaustion of the reserves of some of this coal?

A. No, sir. There are reserves in the Somerset District that are estimated at the present time as 40,000,000 tons, and I am only ascribing production of 8,000,000 tons, I believe it is to the Somerset operation.

Q. Well isn't it true, however, that at the end of forty years some of the workings will have been exhausted.

A. Oh, yes, certain parts of the mine will have been exhausted.

Q. And as you approach that point doesn't the unit cost of operation increase?

A. That depends on the efficiency of the operation. If they got to a retarding basis the much less costs are at the end of operation.

In other words, if you get to the exterior boundaries and mine back, your costs decrease.

Q. Well, isn't there to that extent more shoring and timbering?

A. Not on the completely exhausted, wholly exhausted territory, that in this case would fill up with water. There will be, this Somerset mine has been already partially retarded from the side lines, but the Somerset mine, barring [fol. 1102] unexpected openings, will be in operation on the same unit, that is there is the physical supply after the 40 year period. You see the coal outcrops, there is nothing to stop them making new openings as different places on the property.

Q. Well, have you assumed that your taxes will remain at the present level?

A. Yes, sir; in effect, I am assuming average earnings. There will be fluctuation of other costs, be what they may, and it of course, is not susceptible of in fact determination.

Q. That also involves an assumption of the price of the coal?

A. Yes, sir.

Q. To be realized?

A. Yes, sir.

Q. And what has that assumption been?

A. What has what?

Q. What has that assumption been with respect to the price to be realized?

A. That its relation to the cost of production will remain constant, your ratio of margin of profit between the two that I use now.

To put it another way, if coal is an essential and it is going to be produced, it will be produced at a profit, and [fol. 1103] if the cost of producing it goes up the cost that is obtained for that product will also go up proportionately.

Q. That is an assumption?

A. Well, that is the experience in the past.

Within the range of my experience coal used to sell for $1.00, 98 cents, $1.05 a ton and yield a profit. Of course, in fixing the value, going into any such future period as 40 years, outside of the matter of reserves, the whole question of value resolves itself into one of judgment as to what is going to be returned in the way of profit.

There is no exact method.

Q. Have you considered the possibility that the cost of production may rise to such point that this coal will be no longer commercially valuable?

A. Oh, that has been in my mind. Of course, if it is true there it will be true over the whole United States; costs are comparable.

Q. You had in mind that a substitute would be found for this in other fuels?

A. That is possible. And of course, when you go to consider that, there is the thought that our future source of oil will be from coal. With the increase in the value of crude oil, I think that we will turn to distillation of coal [fol. 1104] or liquifaction of coal.

Q. Is the coal in this field susceptible to that treatment?

A. Yes, sir.

Q. You spoke of assessed values as some test of the estimates you have made. Do you in your work generally regard assessments, or assessed values as any fair criterion of value?

A. In regard to coal mines in Utah, yes, sir. The taxing structure has been worked out rather carefully and the amount recoverable reserves have been worked out very carefully during the last sixteen years, and answering that questions, the taxation of coal mines is rested on rather sound factors.

Examiner Kirby: That is all.

By Examiner Boyden:

Q. In your study of the value of the property of the Utah Fuel Company, as I understand it, you have ventured to indicate that that represents the value of the stock of the Utah Coal Company, is that correct?

A. Well, the values that I have recited here, plus the subsidiary companies, I assume is the value of the stock. Now, I am not an accountant, but I assume that what the

property is worth as represented by so many shares of stock, that represents the value of the stock.

[fol. 1105] Q. Well, what kind of a value would that be, would it be intrinsic value or the exchange value of the stock, or either?

A. Well, what I have tried to do in this report is to fix a value of the property at such a figure that a willing buyer would pay that much for the property.

Q. And you are referring to the property and not the stock, is that correct?

A. Yes.

Q. Is that correct?

A. Yes.

Q. This property in the past has furnished coal to the Rio Grande, has it not?

A. Yes, sir.

Q. Do you recall whether or not that coal has been furnished at the reduced price or whether it has been furnished at commercial prices?

A. Of late years at least I think it has been furnished at the commercial price.

I have that schedule here, if you desire me to read it, but it is the commercial price.

Examiner Boyden: No, I do not care for it.

By Examiner Boyden:

Q. Well, it is true, is it not, that the production of the company in the past has been affected by the demand, [fol. 1106] affected to some extent by the demand; of the railroad for coal?

A. Yes, sir.

Q. And your determination of the value of the property really reflects that demand because it is based on the production of the company, that is true, is it not?

A. Yes, sir.

Q. And the proportion which that is of the total production in Utah?

A. Yes, sir.

Q. In view of the fact that that production has been affected by the railroad demand, is it proper to consider that the prices that you will get for the property is a commercial price?

A. I think so, for this reason: That in modern practice the coal orders from a railroad, at least in our field, are apportioned very largely among all of the producers in that field.

In other words, the railroad is not buying from only one mine all of its coal or nearly all of its coal. They spread their railroad orders around pretty closely in proportion to the output of the mine.

Of course, that was not true in any early day.

Q. Well then, you think that the value of this property which you have stated supports a fair indication of the fair exchange value of the stock, as I understand you?

[fol. 1107] A. Yes, sir, that is my idea.

Q. I am wondering if a purchaser of stock, or contemplated purchaser of the stock would give such consideration as you have to the possible production of the property for the next forty years.

A. Well, that is going a long ways into the future. That is the usual span of life in valuing coal properties that is used.

Q. Well, if you were purchasing the stock wouldn't you be inclined to consider the production of the company and its earnings over recent years and give that greater consideration than you would for in the future?

A. Yes, and in the compilation of my figures I have taken their new money earned since 1928.

Q. Well, if I understand your figures correctly, you have taken an average that runs 40 years ahead at the present time, haven't you?

A. Oh, yes, yes.

Examiner Boyden: Are there any further questions?

Mr. Nicodemus: I would like to ask one or two questions, Mr. Wyer?

Mr. Wyer: Yes.

By Mr. Wyer:

Q. Mr. Burdick, on page 11 of your report you say that in 1929 the natural gas line was completed in Salt Lake City. Do you know exactly in what month in 1929?

[fol. 1108] A. No, I do not.

Q. You do not know whether it was early in the year or late in the year?

A. On one of the graphs here it shows that graphically. My recollection is that it was late in the year, Mr. Wyer. From the placement of the letters "Advent of Natural Gas" in reading to the top of the page, I would judge from its position that it was along late in the year of 1929.

Q. Have their been other parts of the territory served by the Utah Fuel Company where natural gas has come in in recent years?

A. Well, you mean in Utah?

Q. In other parts of the territory than Utah.

A. Well, they have had the natural gas, of course, in California, and in Colorado, but it comes from that Calumet Fuel Company over in Colorado very largely.

Q. Do you know when natural gas was brought into Colorado?

A. No, I do not, I haven't the date.

Q. Now, on page 21 of your report, near the bottom of the page you say "the output of coal in Utah has been seriously curtailed by three main factors," and the first factor is "the wealth of cheap oil from Texas and Cali-[fol. 1109] fornia." Do you know when those factors began to be effective on the output of coal in Utah?

A. Well, there was a time in California when they were quite an interference, prior to 1921. Then shortly after 1921, about 1923 or '24 the West Texas fields were opened up and then began another great interference with the coal business.

Q. Has that continued since that date?

A. Yes, sir.

Mr. Wyer: That is all.

Examiner Boyden: Any further questions?

(No response.)

Any re-direct?

Re-direct examination.

By Mr. Fitzgibbon:

Q. Mr. Burdick, Mr. Hoffman asked a question in regard to the value to the company in its old customers and you went on and spoke of other aspects of it on this whole question.

Has this company benefited by its age and its connections in the field?

A. Yes, sir.

Mr. Fitzgibbon: That is all.

Examiner Boyden: Witness excused.

(Witness excused.)

[fol. 1110] Mr. Fitzgibbon: Now, I would like to call Mr. Korte.

Examiner Boyden: Any objection to Exhibit No. 253?

(No response.)

Received.

(Exhibit No. 253, Witness Burdick, was received in evidence.)

[fol. 1111] WITNESS WILLIAM WYER

By Mr. Marsh:

Q. Mr. Wyer, can you tell me whether or not it is true that half of the common stock of the Denver and Rio Grande Western is held by the Railroad Credit Corporation as pledged by the Missouri Pacific, and one-half is held by Reconstruction Finance Corporation as the pledge of the Western Pacific?

A. That is correct.

Q. Through voting trust?

A. That is correct.

Q. And substantial amounts of the preferred stock are similarly held?

A. Yes.

[fol. 1112] RENEWAL OF MOTION TO STRIKE

Mr. Nicodemus: Well, before we proceed to call witnesses, I would like to offer a further motion.

The Debtor renews its motion submitted at the last session, to strike from the files the reports of the Bureau of

Accounts and the Bureau of Valuation, stated to have been filed herein under Paragraph 11, of Sub-Section C of Section 77 of the Bankruptcy Act, on all grounds heretofore stated, and on the further ground that any document having the evidenciary value prescribed by said Paragraph 11 [fol. 1113] must be introduced at a formal hearing and by a witness whom all parties have a constitutional right to cross examine.

Examiner Boyden: The motion is denied.

Mr. Nicodemus: The Debtor excepts to the denial of the motion to strike the documents from the file, and also excepts to the denial of the adjournment.

In view of the denial of the motion to strike the documents from the files, the Debtor now requests the Commission to tender for cross examination by all or any parties in this proceeding, the following witnesses attached to the Commission's Bureau of Valuation:

Robert W. Lacey, Head of the Accounting Section, George S. Douglass, Engineer attached to the Engineering Section.

Examiner Boyden: Of course, those two individuals have never been presented as direct witnesses in this proceeding.

Mr. Nicodemus: That is one of the defects, we think, that underlies the filing of these documents, that they have not been presented by witnesses who——

Mr. Anderson: Have you made the point that they are not presented by witnesses?

Mr. Nicodemus: I have.

Mr. Anderson: And have you raised the question as to [fol. 1114] who the witnesses are?

Mr. Nicodemus: Not as yet; I have asked them to tender these two witnesses for cross examination. I understood that perhaps some other parties to the case had other witnesses that they would like to have tendered for a similar purpose, is that correct?

Mr. Anderson: Mr. Examiner, at the former hearing the question of calling the representatives of the Bureau of Accounts and the Bureau of Valuation was briefly discussed. At that time the presiding examiner made the statement that in such event they would be called as witnesses for the party calling them. I rather acquiesced in that point of view when I was on my feet at the time.

Upon further consideration I have reached the conclusion that that is not sound, that this evidence is presented by the Commission and not by us, and I am inclined strongly to the view, and respectfully submit for your consideration, that if the request is made or the evidence is challenged, that the Commission produce such witnesses as it may deem necessary to present the evidence in a legal way and then to give us the right to cross examine.

If, on the other hand, and I wish to withdraw any state- [fol. 1115] ment I made on the record to the effect that they would be our witnesses.

On the other hand, if that is not done, it seems to me they should be called for cross examination. I am very reluctant to raise technical questions either of procedure or of law before the Commission, but, as we all know, this case ultimately goes to the Court and the situation there is rather different than it is before an administrative body like the Commission, and therefore I would like to have the record straight on that question, and it is our desire this morning and we again would ask the Commission to call Dr. Wylie, the Head of the Bureau of Accounts, as I understand it, and Mr. Douglass, who has also been called by the Debtor.

We would like an opportunity to cross examine these two gentlemen under such regulations, and under such conditions as you may rule, but I have stated my own view on the situation on the record.

Examiner Boyden: But do you desire a definite ruling as to whether those witnesses will be your witnesses or the Commission's witnesses, before you proceed?

Mr. Anderson: Well, I think it would be desirable to have a ruling on that point, so that we may know the status, but [fol. 1116] if they were called as our witnesses I think we have undoubtedly the right to conduct a cross examination as distinguished from direct.

Examiner Boyden: Well then, the ruling is that witnesses are not Commission witnesses but that you should proceed to present them as your own witness if you desire to produce testimony to rebut the presumptions of accuracy of the Commission's reports.

Mr. Anderson: You will permit an exception to that ruling for the record?

Examiner Boyden: The record shows an exception.

Mr. Nicodemus: And exception on behalf of the Debtor.

The Debtor now requests that the three witnesses be called in the order that counsel may agree upon. I think perhaps Dr. Wylie should be the first witness.

Mr. Anderson: Is Dr. Wylie here, I think he is.

Mr. Nicodemus: He is, and I would like to have the record show that these witnesses are not called by the Debtor voluntarily, but are called by the Debtor involuntarily and under the duress of the Commission's ruling to which we have excepted, and that they are to be regarded as adverse witnesses which the parties to the cause have a right to cross examine.

Mr. Anderson: I think my position and exception are [fol. 1117] sufficiently stated on the record.

* * * * * * * *

[fol. 1118] Mr. Nicodemus: I may say that since the adjournment before lunch, I have conferred with our associates and we agree that it would not be a useful thing to do to offer any evidence here on the seven or eight or more volumes that constitute the underlying data in respect of which we requested full information.

In reliance upon the statement that the Debtor and its counsel would be given free access to the underlying data in the office of the Bureau of Valuation, including the full and free disclosure on its part of all prices that underlie the multipliers, we excused the witness.

Examiner Boyden: Are there any other questions from Mr. Douglass?

(No response.)

Mr. Douglass is excused.

* * * * * * * *

[fol. 1119] Frank C. Squires was sworn and testified as follows:

Direct examination.

By Mr. Nicodemus:

Q. Mr. Squires, will you state your full name and your present occupation?

A. Frank C. Squires; Valuation Engineer; Association of American Railroads.

Q. How long have you been identified with railroad valuation problems?

A. Twenty-five years or so.

Q. Have you been actively engaged in valuation problems in the last year?

A. Yes, sir.

Q. Have you had special opportunity to study the price trends?

A. Yes.

Q. In connection therewith?

A. That is part of my work.

Q. How do the 1935 period prices compare with the spot prices in materials and supplies and other elements that enter into the value of railway property?

A. As of today?

Q. As of today.

A. Those today for most items are substantially higher than those of 1935 and the average value, I think, is today [fol. 1120] substantially higher than as of 1935.

Q. If 1937 spot prices were applied to the units that enter into the inventory of the Denver & Rio Grande Western Railroad, would the value of those—would the application of those prices produce a different result, substantially different result from that set forth in the valuation report filed by the Commission that is under discussion in this proceeding at this hearing; I refer specifically to the item, cost of reproduction new, $168,729,747 that has been referred to by the previous witness?

A. Yes, present day prices would produce substantially more than that amount, assuming that my understanding of how those prices were derived, those prevailing in 1935, is correct.

Q. Those differences will run into many millions of dollars?

A. Yes, sir.

Mr. Nicodemus: That is all.

Examiner Boyden: Do you know whether those prices used in preparing that Bureau of Valuation estimate was spot or period prices?

A. I understand from the exhibit and the explanation they are period prices.

Examiner Boyden: And the prices to which you have testified, that is, the 1937 prices, that is a spot price?

[fol. 1121] A. Yes.

Examiner Boyden: A price applicable in the year 1937 only?

A. Yes, price of today, or the last two or three months.

Mr. Nicodemus: That is all I have.

By Examiner Kirby:

Q. Have you worked out the application of the 1937 spot prices to the D. & R. G. W. inventory as is reflected in the Bureau of Valuation report?

A. No, sir.

Examiner Kirby: That is all I have.

Mr. Nicodemus: Thank you very much.

Examiner Boyden: You are excused.

(Witness excused.)

Examiner Boyden: Mr. Powers is here now.

Mr. Nicodemus: Mr. Powers.

Lawrence L. Powers was sworn and testified as follows:

Direct examination.

By Mr. Nicodemus:

Q. Will you give your full name for the record?

A. Lawrence L. Powers.

Q. You have stated your name; will you now state your occupation?

A. Head accountant and auditor, accounting section, Bureau of Valuation, Interstate Commerce Commission.

[fol. 1122] Q. You are appearing here as a witness in substitution for Mr. Lacey?

A. Yes, sir.

Q. Are your familiar with the document dated March 1, 1937, described as report of the Bureau of Valuation on matters as of December 31, 1935, affecting the Denver & Rio Grande Western Railroad Company and its subsidiaries?

A. Yes, sir.

Q. On page 3 of this report, sheet 1, at the head of the page is an item, "Denver & Rio Grande Western Railway Company, original cost $142,800,512." Will you state from what data and by what process the figure of $142,800,512 was arrived at; by what process and from what underlying data, or the other way around, what underlying data and by what process?

A. With respect to road items and general expenditures, we started with cost of reproduction in the basic valuation in 19(a) cases, and to that we have added the amounts reported by the carrier through order 3, and deducted the retirements reported by the carrier through Order 3, up to and including 1932.

For 1933, 1934 and 1935, we used the gross debits and credits which came from the carriers' records. Now those costs they represent were built up by the Valuation Section. [fol. 1123] For equipment, we started, in the case of the Denver & Rio Grande Western, with the Order 8 costs as reported by the Commission in the final 19(a) valuation reports, adding to those costs the costs reported under Order 3 for equipment and additions and betterments added, less the amount reported under Order 3 for the equipment retired.

Q. That completes your answer?

A. I think that completes the answer.

Q. Well, then, I understand from your answer that this is purely an estimate based upon reproduction value on certain price levels and is in no way related to or in any way based upon evidence of original cost.

A. Well, of course, the original cost at the date of basic valuation, we did not have, and we have used the cost of reproduction as at date of basic valuation as the beginning point on basis of decisions of the Commission in the Roscoe, Snyder & Pacific Case, and various other valuation dockets.

Q. Now, is it not a fact, however, that there was evidence of unquestioned character as to the actual original cost of many items that enter into this property which were not used by the Bureau?

A. There might have been evidences of original cost to date of certain pieces or classes of property in the basic [fol. 1124] valuation that were not considered in our figures.

Q. Well, isn't it a fact that that evidence was rejected and the estimate that you have described substituted, regardless of the fact that the evidence of actual cost would have produced a higher figure than the estimate?

A. Not to my knowledge, I do not know anything about rejecting anything.

Q. Well, it is true, is it not, that the entire figure is based upon the estimate that you have stated here in the docket?

A. Well, when we start out with the date of valuation, not the entire figure, no, but the portion of it that applied to road might be called an estimate, but by the time the retirements from the inventory are deducted from that amount, at the end of 1925, 64 per cent of that total, 64.4 is actual and 35.6 per cent is estimated.

Q. Well, the entire inventory, as it existed at 1919 was—the entire original cost as of that date was estimated on the basis of 1910-1914 prices?

A. That is right.

Q. Now, I will ask you whether you can furnish, in the form of an exhibit, an analysis of the item of $142,800,512 to enable the parties to this proceeding to check the computation?

A. Why, we could do that if the Examiner so rules, but [fol. 1125] it would be quite a voluminous exhibit. The details are all available for examination.

Mr. Nicodemus: He has made a similar ruling in connection with the reproduction new, and I simply asked to make the record.

Examiner Boyden: How long would it take to prepare it?

A. It would take several weeks, I think, to prepare it in the form of an exhibit.

Examiner Boyden: Are you asking that it be prepared?

Mr. Nicodemus: We ask that it be prepared in the form of an exhibit.

Examiner Boyden: The request is denied. We will receive any evidence that you have to offer at this time, understand, Mr. Nicodemus, and Colonel Anderson.

Mr. Nicodemus: I thank you.

Examiner Boyden: And the underlying data relied on are used by Mr. Powers and the accounting section will be made available for your examination in the offices of the Commission.

Mr. Nicodemus: At convenient times, between now and the time this case is submitted?

The Witness: Yes, and after that.

By Mr. Nicodemus:

Q. In the descriptive statement that appears on page 5 of the report of the Bureau, reference is made to the in-
[fol. 1126] clusion of subsequent additions and retirements as adjusted, ascertained from reports of the carriers under valuation order No. 3, and so forth. Will you indicate the nature and the extent of the adjustment to which reference is there made?

A. Well, those adjustments would consists of any exceptions which the Section would take either to the additions or the retirements or in the way of retired property that had not been retired, or excluding the additions that were not considered as original cost to date, and such things as that.

Mr. Nicodemus: We have a detail of all of those exceptions.

Q. Will you prepare and submit in exhibit form a memorandum showing the adjustments that are referred to on page 5 of the Bureau's reports?

Examiner Boyden: How long will that take, Mr. Powers?

A. It seems to me, Mr. Examiner, that that could very easily be checked in connection with the examination of the underlying record and we could not only explain it but help the carriers' representatives in pointing these things out.

Examiner Boyden: How long would it take to prepare the exhibit, approximately?

[fol. 1127] A. The exhibit of the exceptions, probably be a week or ten days.

Examiner Boyden: The request is denied. The information is available to counsel.

By Mr. Nicodemus:

Q. Mr. Powers, are you familiar with the property of the Denver & Rio Grande Western Railroad Company and its subsidiaries?

A. By actual experience?
Q. By actual experience.
A. No, sir.
Q. Are you familiar with the tie situation?
A. No, sir.
Q. Well, if you were advised that the original ties had been practically entirely replaced by treated ties, and I will have that covered by the next witness; could you state whether the cost of the treated ties, the excess cost, is reflected in the item of original cost as reported in the documents we have under consideration?
A. Yes, I can answer that by saying they are not.
Q. They are not? Thank you.
A. Under ruling of the Commission.

Mr. Nicodemus: That is all we have with this witness.
Examiner Boyden: Any cross examination?
Mr. Anderson: I understand that in your opinion the [fol. 1128] original valuation, 1919, was, for ratemaking purposes, based on 1910 to 1914 prices, wasn't it?
A. The report so states, for ratemaking purposes.

Mr. Anderson: That is all.

[fol. 1129] MOTION TO STRIKE

Mr. Anderson: In order to make the record clear I want to submit a motion. First, as to the report of the Bureau of Accounts, and second, as to the report of the Bureau of Valuation.

I wish to move to strike out so much of the report of the Bureau of Accounts as deals with items other than those included under the heading, "Schedule 1a: Modifications necessary to correct accounting not in conformity with the Commission's regulations."

That is, I do not move to strike out those modifications, but I do move to strike out that portion of the report under the other three headings in the schedule in italics in the court record.

I wish to make the same motion with respect to the other railroads other than the Denver, applicable to the same items, which I think are sufficiently described, and for grounds of that motion I desire to state (1) that the report

of the Bureau of Accounts is not made in conformity with [fol. 1130] the requirements of Section 77 of the Bankruptcy Act,

Examiner Boyden: In what respect, Colonel Anderson?

Mr. Anderson: Do you want me to argue the question, sir?

Examiner Boyden: I should like for you to say in what respect.

Mr. Anderson: I just simply say that the Bankruptcy Act requires a report on the accounts of the company and not on a theoretical hypothesis of what they might be ten or fifteen years from now in the light of new conditions.

That is one ground, and others I might state, I do not want to argue the question.

In the second place, the reports are incorrect in facts, incomplete and highly prejudicial to the rights of the parties in this case and are not, therefore, admissible as evidence.

Examiner Boyden: When you say they are "incorrect in fact" you refer to the facts set forth in the testimony heretofore?

Mr. Anderson: In the reports themselves, which show on their face, as well as in the testimony, that they are predicated upon assumptions as to statutes not in existence and as to other facts not in existence as to the future, and [fol. 1131] that they have undertaken to charge those companies and those accounts with all the losses that they can and credited them with none of the gains.

Examiner Boyden: Are there any incorrect facts set forth in the report which have not been developed on the record?

Mr. Anderson: I do not now recall that there are facts not developed because I cannot carry the entire record in my mind, but I reserve the right to point out at another place than this.

I have in mind the report, that part of the report insofar as it refers to the last three items. I am eliminating now the first item, but the last three items do not deal with facts at all, but deal with hypotheses and assumptions, and that is not evidence.

Examiner Boyden: Well, I merely brought that up because I want it clear that we are ready to listen to you and to any evidence you may have at this time with respect to inaccuracies and incorrect practices in those reports.

Mr. Anderson: I am not in position now, Mr. Examiner, to present any evidence on that subject. I have only the reports themselves, and very brief conversations with the representatives of the Bureau of Accounts, and not a proper examination of the accounts, and if I do have an [fol. 1132] opportunity, after the record is closed, of course, I could not put that in evidence because that would be my own examination and would be of no benefit to the record. I could not use it in argument, either before the Commission or the courts.

Further, the use of these reports, accounting reports, in the light of the facts disclosed by this record as basis for determining a sound and equitable plan of reorganization, or as affecting in any way the rights of our clients, the insurance group, and the other parties of interest in this case, would be in effect, taking into consideration the method in which they have been prepared, a denial to them of due process of law and in violation of their constitutional rights to the protection of their property under the Federal Constitution and amendments thereto, and especially in effect a taking of their property for public use without just compensation.

For these and other reasons which I reserve the right to urge, I desire to submit the motion for the dismissal of the reports of the Bureau of Accounts as to all the properties involved in this proceeding.

I recognize that the reports having been filed by order of the Commission, the Examiners cannot grant this motion, but I put the motion on the record for the purpose [fol. 1133] of arguing it before the Commission, before the court, or any other forum at another appropriate time, until this case is finally disposed of in whatever forum it may go.

Off the record.

(Discussion off the record.)

Examiner Boyden: I that all the motions you have with respect to the reports?

Mr. Anderson: The accounting reports, yes.

Examiner Boyden: Of the reports of the Commission?

Mr. Anderson: The accounting reports: I then want to make a motion with respect to the Bureau of Valuation.

Examiner Boyden: Well, the motion with respect to the reports of the Bureau of Accounts is denied.

Mr. Nicodemus: Prior to the denial of that motion, I would like to unite in it on behalf of the Debtor and its subsidiaries.

Mr. Anderson: Now, with respect to the report of the Bureau of Valuation filed with respect to the Denver & Rio Grande Railroad Company and its subsidiaries, including the Denver & Salt Lake Railroad, I desire to move to strike out these reports from the record in this case upon the ground, among others, that they do not constitute any basis whatever for the valuation of this property in a reorganization proceeding, but are misleading and preju- [fol. 1134] dicial to the rights of the parties in that they undertake to state elements of value without stating what elements of value are involved in a true valuation, and such elements of value are predicated upon price conditions and other factors shown by the record to have been ascertained for the purpose of making a valuation for rate making purposes and not for making a valuation for reorganization purposes, and ascertained more than twenty years ago when the value of the American dollar was different from what it is today and all the other factors entering into the value of property were highly different from what they are today, and the record does not sufficiently disclose the basis of such valuation to enable it to be considered as evidence in this cause.

Second, that the reports undertake to show the depreciated value of this property when there is no depreciation in the property for the purposes of reorganization or for market value, but, it is more valuable today than it has ever been in its history. And they do not take into consideration elements of earnings and other factors of goodwill, and going concern value, which are essential to the ascertainment of the value of this property and the issue of the securities thereon.

That the reports are in other respects defective and prejudicial to the interests of the parties whom I repre- [fol. 1135] sent, and are not competent evidence as to the rights of any party to this proceeding, and in incomplete form.

Fourth, that if these reports be used or considered as evidence affecting the rights of the parties in this proceeding, it will constitute a taking of the property of the owners of the securities of the Denver for public use, with-

out just compensation, in direct violation of the provisions and amendments of the Federal Constitution.

That the reports have not been prepared in accordance with and do not conform to the requirements of Section 77 of the Bankruptcy Act, and are not admissible in this cause.

Now, as to these motions, I wish to say that I make them with all possible deference to the Commission, with no desire whatever to obstruct, delay or in any way embarrass the administration of the Act or the performance of my duties under the Act, but it is manifest from the reasoning with respect to the use of similar reports in other cases that if these reports are used for the purposes indicated, serious legal and constitutional questions are involved which I feel it is my duty to reserve upon the record and present at the proper time and in the proper forum.

Mr. Nicodemus: The Debtor unites in that motion on be-
[fol. 1136] half of itself and all of its subsidiaries.

Examiner Boyden: Motion denied.

Mr. Anderson: And I wish in that connection to add that I object to the use of these reports as prima facie evidence of any fact in this case, because the evidence discloses they are not based upon facts but upon assumptions.

Mr. Nicodemus: The Debtor and its subsidiaries join in that additional ground for the motion.

Examiner Boyden: The objection is noted.

. . . . . .

[fols. 1137-1138] Witness T. A. Thompson.

By Mr. Anderson:

Q. Mr. Thompson, will you please state your name and your position with the Denver & Rio Grande Western Railroad Company or with the trustees thereof?

A. T. A. Thompson, general auditor.

Q. How long have you been connected with the Denver?

A. 24 years.

Q. You have been the general auditor of the trustees since their appointment in 1935; have you not?

A. No. Since 1937.

Q. 1937. Before that you were connected with the property and also an officer of the trustees; were you not?

A. I was.

Q. As general auditor you have charge, as I understand, of all the accounting services of the trustees and of the property.

A. I do.

Q. Now, I hand you a printed document entitled "Report of the Denver & Rio Grande Western Railroad Company, Wilson McCarthy and Henry Swan, Trustees, Year Ended [fol. 1139] December 31, 1940."

Can you identify that as the annual report issued by the trustees to its security holders for the year 1940?

A. I do.

Mr. Anderson: I would like to offer that in evidence and give it an exhibit number, sir.

Exam. Boyden: That will be Exhibit No. 260.

(Exhibit No. 260, Witness Thompson, marked for identification.)

Mr. Anderson: 260.

By Mr. Anderson:

Q. I understand that the Denver & Salt Lake Railway Company is separately operated by the Denver & Rio Grande Western Railroad Company and is operated by the corporation and not in the hands of trustees. I am correct about that?

A. That is correct.

Q. I asked you to present official report of that company, and I now present you "Fourteenth Annual Report of the Denver & Salt Lake Railway Company, for the Calendar Year Ended December 31, 1940," a printed document, and ask you if you can identify that as a report issued by that company, of your own knowledge, to its stockholders for the year 1940?

A. That is the report.

Mr. Anderson: I off that in evidence as Exhibit No. 261.

[fol. 1140] Exam. Boyden: Marked as Exhibit No. 261.

(Exhibit No. 261, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. Mr. Thompson, I requested the trustees to have prepared under their direction, I presume by you, a statement

separating the D. & R. G. W. operating expenses between freight and passenger business on the ICC basis, developing a 1940 unit cost of operation in terms of gross—of cost per gross ton mile and cost per passenger mile for the years 1936, 1937, 1938, 1939, and possibly 1940.

Have you prepared or had prepared under your direction a statement in response to that request?

A. I have.

Q. This statement entitled "Denver & Rio Grande Western Railroad Company—Wilson McCarthy and Henry Swan, Trustees—D. & R. G. W. earnings estimated on basis of 1940 unit costs," is that the statement in response to the request which I made?

A. That is.

Mr. Anderson: And I would offer that in evidence, sir, as Exhibit No. 263, I think is the number.

Exam. Boyden: Mark it 262.

(Exhibit No. 262, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. That statement is a correct statement of what it [fol. 1141] purports to be, is it not, made under your direction?

A. It is.

Q. Mr. Thompson, during the period of the trusteeship there have been, as appears from this record, considerable expenditures for improvements and betterments to the property carrying large charges to operating expenses incident to or through improvements. You have made no adjustments on that account in making up the statement 262, have you, taking it as——

A. No statements—no adjustments of any kind.

Q. That is right.

Exam. Boyden: How many sheets are there in that statement, Mr. Anderson?

Mr. Anderson: I beg your pardon?

Exam. Boyden: How many sheets are there in that statement?

Mr. Anderson: Only one sheet in that statement. 262 is one sheet. I will have the record show that as to the others.

By Mr. Anderson:

Q. I also asked you to make up a statement for the years 1939 and 1940 for the Denver & Salt Lake, or have them made and present them at this time. Have you such a statement?

A. I do?

Q. You have handed me a statement in response to that inquiry, a paper consisting of one sheet, entitled, "The Denver & Rio Grande Western Railroad Company—Wilson [fol. 1142] McCarthy and Henry Swan, Trustees—D. & S. L. 1936-1940 Earnings Restated on Basis of 1940 Unit Costs."

Q. Is that correct?

A. That is correct.

Mr. Anderson: If so, I will offer that exhibit as the next exhibit.

Exam. Boyden: Mark Exhibit 263.

(Exhibit No. 263, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. What you said with regard to no adjustments as to improvements and betterments made in making up that other statment applies also to that statement?

A. That is correct.

Q. I then asked you to take these two statements and make up a statement showing the earnings of the two properties upon a consolidated basis for each of the five years, and in doing so not to make any—not to include any alleged savings or prospective savings from consolidation if the same was effective, but to make a note to that effect on the statement.

Have you such statement?

A. I have.

Q. You have handed me a statement with a heading as already given on the others introduced, but sub-heading "Combined D. & R. G. W. and D. & S. L. Earnings, 1936-1940, Restated on Basis of 1940 Unit Costs."

[fol. 1143] That is a statement prepared in response to the request I made; is that true?

A. That is correct.

Mr. Anderson: I would offer that in evidence as the next exhibit number.

Exam. Boyden: Exhibit No. 264.

(Exhibit No. 264, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. I also requested the trustees to have prepared a statement being a forecast of net available interest for the D. & R. G. W. in the year 1941. Have you prepared such statement and, if so, will you explain just what it means or is, how it is prepared?

A. This is a statement showing the actual figures for the first three months of 1941 and estimated for the balance of the year and based on the projected work and estimated revenue for the balance of the year.

Mr. Anderson: I present the statement with the general heading indicated above, sub-heading "1941 D. & R. G. W. Income Forecast (three months actual, nine months estimated)" with certain explanatory footnotes which I will offer in evidence as the next exhibit.

Exam. Boyden: Mark it as Exhibit No. 265.

(Exhibit No. 265, Witness Thompson, marked for identification.)

[fol. 1144] Mr. Anderson: I think I should have stated at the beginning and would like to state now that at the hearing in Denver the annual reports of the property and its earnings, statements up through the year 1938 and for as much as was available for 1940, were presented, and I take it is in evidence before the Commission in this hearing, and the annual reports which I presented this morning will bring it up to date. I didn't present the intervening reports because they are all in the record. See, the original record closed in 1936, and at Denver in the hearing there we presented the intervening reports and data and earnings on income, and now these reports presented this morning bring it up to date. I understand all the evidence presented at Denver is before the Commission here.

By Mr. Anderson:

Q. I also asked that you would present a net available for interest for the D. & S. L. for the year 1941. Have you

such statement prepared? This statement, as I take it, is made up in the same manner as the one you previously presented, that is, actual income accounts for the first three months and estimated or forecast for the remainder of the year?

A. That is correct.

Mr. Anderson: The statement which the witness has handed me is entitled "Income Forecast—12 Months Ending December 31, 1941—January to March Actual, April to [fol. 1145] December estimated," with certain footnotes and explanations thereof.

I offer it in evidence.

Exam. Boyden: Mark it as Exhibit 266.

(Exhibit No. 266, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. I also requested a statement—that the statements referred to above, that is, the last two exhibits, be put together on a consolidated basis omitting any estimated savings from consolidation, with a note to that effect. Have you such statement?

A. I have.

Mr. Anderson: The witness hands me in response to the inquiry a statement with the general title and sub-title of "Combined D. & R. G. W. and D. & S. L. Income Forecast, 1941 (three months actual, nine months estimate)."

I offer it in evidence as the next exhibit, sir.

Exam. Boyden: Mark it Exhibit 267.

(Exhibit No. 267, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. I also requested that there be prepared statement showing the extraordinary expenses—scratch that, will you please?

Mr. Thompson, your forecast for the year 1941 also is based upon results including the extraordinary expenditures [fol. 1146] contemplated to be made in that year; is it not?

A. That is correct.

Q. You have not, in other words, adjusted the earnings in any way or the forecast in any way with respect to charges to operating expenses which result from the improvements which the budget calls for during the year 1941?

A. The forecast includes the effect of improvements.

Q. Yes.

Exam. Jameson: How much does that mean? Do you know in a rough way how much that would affect it, what you call extraordinary expenses?

The Witness: I can't give you the accurate figure, the exact figure. I would say a million dollars with charges to operating expenses in connection with improvements.

By Mr. Anderson:

Q. In other words, your improvement program will carry to operating expenses approximately a million dollars of charges?

A. That is correct.

Q. Such as maintenance, and so forth, which you have carried into your operating expenses in arriving at the results shown in the statement you have presented——.

A. That is correct.

Q. —all the way through?

Exam. Boyden: Well, does that million dollars all represent an extraordinary improvement program?

[fol. 1147] The Witness: Not necessarily. In other words, the rail program will take $650,000, $700,000 of it alone: That is a normal rail program.

Exam. Boyden: How much of it would you say was extraordinary?

The Witness: I don't believe I can answer that question.

By Mr. Anderson:

Q. Is it not a fact that you this year on account of the peculiar conditions are accelerating improvements to or repairs to a large number of cars which you had contemplated—the trustees had contemplated deferring over a period of years and, if so, will you state the facts with respect to that, so far as you know them, and by consulting Mr. Bradford?

A. Well, the program this year includes the rehabilitating or rebuilding, probably not complete rebuilding, but the ex-

penditure of $250 or $300 a car on some 14 to 1,500 boxcars that would ordinarily have been spread over a period of 5 years.

Q. I see.

A. Because of the defense program and the prospective need for the equipment, why, the work is going to be done in 1941.

Q. Yes. Now, in other words, you have advanced the expenditures which you would have spread over four or five years as to those cars to be made in the year 1941, and all of that is included—expense incident to that is included in [fol. 1148] making up this forecast, included for this year?

A. Such part of it as is involved in the expenses is in the forecast.

Q. Can you give approximate figures or actual figures as to the amount of extraordinary expense which you will thus advance from future years into 1941?

A. I don't believe I can answer that question.

Q. What is the total amount of the program? Do you know?

A. $765,000.

Q. $765,000. All operating expenses incident to the improvement of those cars?

A. No; there will be some betterments in there.

Q. Some little betterments. But the larger part of that is operating expenses?

A. That is correct.

Exam. Boyden: Well, was that original program over a longer period?

The Witness: It was programmed to be completed in 1945.

Exam. Boyden: When was that program drawn up?

The Witness: In 1937.

Exam. Boyden: And they propose now to do it all in 1941?

The Witness: 1941; on that certain lot of equipment.

By Mr. Anderson:

Q. And in your statement it is affected accordingly——

[fol. 1149] A. It is.

Q. By those operating expenses?

Mr. Anderson: I don't think I have any other questions——

By Mr. Anderson:

Q. Oh, there are two more statements you made there. Have you any other statements to present in accordance with my request?

A. I have.

Q. You hand me a statement entitled—the general heading—"Statement of Actual Expenditures for Road and Equipment (exclusive of retirements) November 1, 1935 to March 31, 1941."

That statement for the Denver & Rio Grande Western was made up under your direction, I take it?

A. It was.

Q. The figures were taken from your accounts?

A. Not 100 per cent, Colonel.

Q. Well, explain the statement.

A. The statement was according to classes, which is not the way it appears in the accounts.

Q. Yes?

A. The descriptions are, as we describe, the former divisions of capital expenditure classifications and not the primary accounts that appear on the books, and this particular setup was drawn off in the engineering department by form practically agreeing with the charges on our books.

[fol. 1150] Q. Now, the statement, however, of the amounts expended is correct; is it?

A. It is, substantially correct.

Q. The classification on the left hand side of the various items being made by the engineering department, but the statement of expenditures for those years for the purposes stated are correct?

A. That is correct.

Mr. Anderson: I will offer that in evidence as the next exhibit.

Exam. Boyden: Mark it Exhibit 268.

(Exhibit No. 268, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. You also hand me a statement made at my request, "The Denver & Rio Grande Western Railroad Company, Statement of Actual Expenditures for Operating Expenses

in Connection With Improvements, November 1, 1935, to March 31, 1941."

That statement was prepared under your direction?

A. It was.

Q. It is a correct statement of what it purports to be; is it?

A. It is.

Mr. Anderson: I offer it in evidence as No. 269.

Exam. Boyden: Mark it 269.

[fol. 1151] (Exhibit No. 269, Witness Thompson, marked for identification.)

By Mr. Anderson:

Q. Mr. Thompson, is it not a fact that the property purchased a very considerable amount of new equipment during the period of the trusteeship?

A. Yes.

Q. Have you got a statement of the amount of equipment so purchased?

A. I have that statement, if I may be the witness on it.

Q. Yes; you have a statement. It was intended to put that in by Mr. Bradford; wasn't it?

A. It was.

Q. And you have made—I will put if in later then. You have made no adjustments in your accounts for the benefits, if any, which have accrued from the use of this equipment or the improvement of equipment which has taken place since 1935; have you? You haven't made any allowance for that?

A. I don't believe I understand your question.

Q. I mean the increased efficiency or anything of that kind. In making up the statements as made for you, you have taken the cost as shown by your records?

A. That is correct.

Q. You haven't made any allowances for anything of that kind?

A. I have made no adjustment.

Q. I note in Exhibits 262 and 263 that hire of equipment [fol. 1152] for the years '36 and '39 were as reported and not restated to be the same as in 1940. These rentals were considerably less than in 1940, weren't they—were considerably less in 1940, weren't they, on account of the increased equipment and the increased improvement in equipment?

A. In the 1940 figures hire of equipment, net, was less than the preceding years, giving the effect of the new equipment on which per diem was earned.

Mr. Anderson: That is right. I think that is all.

Exam. Boyden: Cross examine.

Mr. Clay: I have some questions.

Exam. Boyden: Mr. Clay.

Cross-examination.

By Mr. Clay:

Q. Mr. Thompson, you testified that the trustees contemplated spending within the months ending at the end of the year $250 or $300 a car on some 1,400 cars.

A. Correct.

Q. Is that for the installation of A. & B. brakes?

A. It does not include A. & B. brakes.

Q. Well, if it were not for the defense program, would you have any need for those cars?

A. I would say not at this time, not in the complete volume.

Q. Is it not also true that any increased expense for the reconditioning of those cars will be offset by what profit you make on the increased business due to the defense pro-
[fol. 1153] gram?

A. I assume so.

Q. That work was not in the trustees' original rehabilitation program; was it?

A. It was in the program that was set up about four years ago for increasing and improving equipment. These 1,400 cars were scheduled for rehabilitation over a period of five years starting in 1941.

Q. You just testified that there would be no need for those cars except for the defense program. Certainly the trustees would not have spent the money if they couldn't use the cars; would they?

A. Well, I intended to convey the impression that in an orderly manner they would be required over a period of five years. In other words, 20 per cent of them would be required in 1941.

Q. Now, you testified that the improvement program during 1941 will increase operating expenses about a million

dollars. Will you break that down? How did you arrive at that million dollar figure?

A. I am picking that for you pretty much out of the air because I don't know what the exact figure is.

Q. Is that a figure you have arrived at since you are here in Washington, or is it a figure which the trustee has given you?

[fol. 1154] A. I made the figure right here in Washington.

Q. On what basis? And would you explain the basis of the figure?

A. I have stated it was purely an estimate and it includes the operating expenses in connection with the laying of 60 miles of rail.

Q. Well, take that one item. That is rail that you re-lay ordinarily; isn't it?

A. That is correct.

Q. That is the——

A. That is correct.

Q. Now, how much of the million dollars is due to the re-laying of 60 miles of rail?

A. Half a million dollars.

Q. That is just ordinary maintenance; isn't it?

A. Well, it is, to the extent that rail is considered ordinary maintenance. The accounting—the regulations of the Commission require that the cost of the increase weight be capitalized.

Q. Well, a half a million dollars of this cost is reflected in operating expense because of re-laying the rail?

A. That is correct.

Q. The trustees don't plan any more work on roadway, do they, of any consequence besides the re-laying of that rail?

A. Well, there is a rather extensive program of bridge [fol. 1155] work and culvert work that is under-way.

Q. Well, that is just ordinary work, isn't it, that you do ordinarily?

A. That is correct, about a normal program.

Q. Normal program. Such as you would have to do in any future year with this level of business?

A. Approximately that.

Q. Now, that accounts for a half a million dollars of it. Could you give me the basis of the—on which you estimated the remaining half a million dollars?

A. On the—I have figured in connection with that rehabilitation of 1,400 cars there would be some capital expenditures and, therefore, if it was capital you have to have authority for it and the operating expenses would be carried in connection with the improvements.

Q. That is, improvements to equipment?

A. That is correct.

Q. The remaining half a million dollars is for improvements to equipment?

A. That is correct.

Q. And the 1,400 cars. Is there anything else?

A. Offhand, I can't answer your question.

Q. Are you going to do any improvement work on locomotives such as——

A. No major jobs on locomotives, no.

[fol. 1156] Q. Any major installations of automatic stokers?

A. Just the usual program. I think there are 10 stokers scheduled for this year.

Q. That would be just normal installation?

A. Well, it would be to the extent necessary to get the program completed by the time all locomotives have to be equipped with stokers under the law.

Q. When is that date?

A. 1945, I believe.

Q. You are not going to complete your installation of automatic stokers; there will be some locomotives remaining, won't there, to be so——

A. There will be some locomotives remaining——

Q. —equipped in future years?

A. —if they are used in main line service which would have to be equipped with stokers, but they are not being used in main line service at the present time.

Q. Well, you are not equipping more locomotives than you need in connection with the estimated business you will have under the defense program?

A. All the modern locomotives come equipped with automatic stokers, and we have remaining only one class that requires automatic stokers to be operated in main line service, and that one class is not ordinarily used in main line service. We might have to use them with the influx [fol. 1157] business this fall or in 1942.

Q. If you run into a traffic peak?

A. That is correct.

Q. Now, would you be good enough to turn to your Exhibit No. 262?

Now, as I understand, what you have done on this exhibit is merely to carry out the wish expressed to you by the insurance group as to the way this exhibit would be made up. The trustees do not sponsor this——

A. They do not.

Q. —basis on which the exhibit is made up?

A. They do not.

Q. You just administerially have projected these figures in accordance with the request made of you?

A. That is right.

Q. And the same is true of exhibits 263 and 264?

A. 263—263, yes. 264 is a consolidation of 262 and 263.

. . . . . .

[fol. 1158] Is it not true that your best prospect of the increased business above the 26 million and a half gross will be from the further development of bridge traffic?

A. I think that is correct.

Q. And is it not also true that the bridge traffic is a kind of traffic that, speaking generally, will return low revenue because it is competitive with the bridge traffic that the Union Pacific and the Santa Fe carry.

A. I don't think the fact that it is competitive has anything to do with the revenue. The rates on a ton-mile basis on long-haul traffic are naturally lower than on short-haul traffic.

. . . . . .

[fol. 1159] WITNESS R. K. BRADFORD

By Mr. Anderson:

Q. Will you please give your name and position, where you live, and position with the Denver & Rio Grande Western Railroad or trustees thereof?

A. R. K. Bradford; residence, Denver, Colorado; assistant general manager of the Denver & Rio Grande Western.

Q. How long have you been connected with the Denver, Mr. Bradford?

A. Since August, 1923, with the exception of one year when I was loaned to the RFC.

Q. You have been in the railroad business practically all of your business life; haven't you?

A. Yes, sir; all of my business life, since 1913.

Q. I asked the trustees of the Denver to supply a witness and they suggested you as a probable witness to testify to certain specific matters which we felt might be helpful in this case in arriving at reorganization, and I will ask you as to the questions which I submitted to them and get you to answer them in your own way.

First, I will ask you if you have a statement showing the principal items of new equipment acquired by the Denver from November 1, 1935, to December 31, 1940?

A. I have.

Q. Is the statement which I hold in my hand the one to which you refer?

A. Yes, sir.

[fol. 1160] Q. That does not purport to show, I take it, all of the equipment acquired, but it does show the principal items acquired?

A. Well, it shows the principal items up to December 31, 1940. There have been other items acquired since that time, though.

Q. Well, now, will you state what have been acquired since then or what is on order at this time?

A. There has been acquired since December 31st, 1940, 500 additional boxcars, the same type and capacity of the 900 acquired prior to December 31st, 1940. There has been ordered 14 Diesel switching engines the delivery of which will start this week. There has been ordered and received one Diesel switching engine which at the present time is being used two-thirds of each 24 hours by the Rio Grande and one-third in the so called Associated Railway Service protecting the Remington Arms plant at Denver. The engine is in the service of the Rio Grande, Santa Fe, Burlington, C. & S. and Rock Island. Authority has been given and material has been ordered for the rebuilding of 100 additional stock cars, for the building of 10 additional cabooses. Authority has been given and the court is being petitioned for authority to build or buy 100 flat cars to replace flat cars that have been worn out. Five

additional 4664 Mallet locomotives similar to our 3700 series that were bought in 1938 have been ordered and will be delivered, we are promised, in October. Three 5400 horsepower Diesels have been ordered, and we are promised [fol.1161] delivery in January and February, 1942. That will take care of all of the equipment which has been purchased since 1940 or which has been authorized since that time.

Q. Since November 1, 1935?

A. Yes, sir.

Q. In other words, taking this statement which you hand me entitled "Principal Items of New Equipment Acquired, November 1, 1935-December 31, 1940," and adding the equipment which you have enumerated in your testimony would give the principal items of equipment acquired by the railroad from the beginning of the trustee—acquired or ordered by the railroad from the beginning of the trusteeship down to the present time?

A. That is correct, sir.

Mr. Anderson: I will offer that in evidence as Exhibit No. 270, I think it is.

Exam. Boyden: Mark it Exhibit 270.

(Exhibit No. 270, Witness Bradford, marked for identification.)

Exam. Boyden: Are you able to give us any information about how much of this equipment has been paid for and how it was acquired, whether by equipment trusts or otherwise?

The Witness: All of the so called purchase items, with the exception of the seven tank cars and, I believe, the 14 units of work equipment, were acquired on equipment trust. [fol. 1162] The seven tank cars are actually tank cars that we bought as individual cars, second hand or that were damaged or something, and converted into water cars.

Exam. Boyden: Those have been paid for?

The Witness: Those have been paid for. The converted cars all were taken care of out of current expenses. The built cars, that is, the 300 stock cars, the 20 cabooses, the passenger and automobile cars were all built or rebuilt in our shops and paid for currently.

Exam. Boyden: Did you include the rebuilt cars in that?

The Witness: Yes, sir. The rebuilt passenger cars and

the rebuilt 78 automobile cars were taken care of out of our current expenses.

Exam. Boyden: And also the built cars?

The Witness: Yes, sir.

Exam. Boyden: Pardon me. How about the other equipment that you mentioned that has been ordered?

The Witness: Well, the one Diesel that is used in the so-called Associated Railroad Trade at the present time is being handled on the lease purchase agreement that we have suggested to the other railroads, because there are five more or less involved, that we all pay cash for it and then adjust the ownership after the Remington plant is credited up.

Exam. Boyden: Have there been any payments made on that?

The Witness: Yes, sir; February, March and April. [fol. 1163] Exam. Boyden: What are the monthly payments?

The Witness: $877.50, sir, in principal, and the interest starts at about $75 a month and decreases each month.

Exam. Boyden: What is the total cost of that?

The Witness: $78,000.

Now, the 14 Diesel switch engines, one of them being purchased from the General Electric Company; that is a small 380-horsepower Diesel, we will pay cash for that. Of the 13, there *is* nine 360-horsepower being purchased from the Baldwin Locomotive Works; four 100-horsepower being purchased from the American Locomotive Works, and those we will pay 25 per cent cash and the balance over 90 months, I think.

Exam. Boyden: And what is the total cost of the 14 units?

The Witness: Well, I will have to do a little adding here. We will have $675,000 in that equipment trust on those 13 units. The 380-horsepower cost us $36,000 and will cost us $200 or $300 to get out to us.

Exam. Boyden: That is for each of them?

The Witness: That is for the one that we are buying cash from the General Electric. The 660-horsepower cost us $68,500 f.o.b. factory, and the others $78,000 f.o.b. factory. There are four of the 1,000-horsepower; nine 660-horsepower. Those are being paid for 25 per cent cash and the balance spread over 90 months payment. The new [fol. 1164] steam locomotives which will be delivered in October and the three Diesel electric freight locomotives

which will be January and February delivery are all going to be handled on an equipment trust. I can't tell you exactly what will be paid down and how that will be spread. It will be probably on a mixed sale.

Exam. Boyden: What is the total cost?

The Witness: The Diesel locomotives will cost us $500,000 apiece, or $1,500,000, and the other locomotives will cost us $232,000 apiece, or $1,160,000. That is f.o.b. the plant. It will cost us something to get them out there.

By Mr. Anderson:

Q. You have got about $4,000,000 of equipment on order now, in round numbers?

A. Yes, sir.

Q. Now, Mr. Bradford, I asked that you be prepared to testify to the improvement work which has been done by the bankruptcy trustees during the trusteeship of the Denver. First, the amount of money spent. That statement of the amount of money spent was put in by Mr. Thompson this morning, I think; wasn't it?

A. Yes, sir.

Q. As one of the exhibits. Now, can you describe generally the character of the improvement and where it is done and make any statement on that subject that you think will be helpful in arriving at what has been done by the [fol. 1165] trustees in the improvement and development of this property, generally?

A. Of the approximately $17,000,000 that has been spent in improvements and charged to road and equipment in the period January 1 to March 31, 1940, approximately $9,000,000 covers new locomotives and freight cars. There is another million and a quarter that has been expended in improvements to existing locomotives, that is, locomotives that the trustees found on the property, locomotives and cars. The next biggest item is in rail and other track materials on which we have spent approximately a million and three-quarters dollars and approximately a million dollars on bridges.

At additional yards and sidings there have been about $900,000 spent. Practically speaking, all of that expenditure has taken place on the line between Denver and Ogden via the tunnel and via the gorge. In other words, the greater proportion of this money has been spent for equipment or

power, for rail or bridges, ballast, yard improvements, shop facilities, and improvements on the main line of the railroad. There have been some improvements on the back lines, of course, by reason of rail being shoved back on those territories, but primarily the expenditure has been concentrated on the main line railroad.

Q. That statement shows the amount spent on roadway and structures as well as on the other items you have men-
[fol. 1166] tioned; doesn't it?

A. Yes, sir.

Q. The total amount?

A. $7,666,756 in roadway and structures. $9,837,490 R. & E. on equipment.

Q. This, of course, does not include any operating charges or betterments——

A. No, sir.

Q. —in either roadway and structure or equipment?

A. The operating expenses on roadway and structure have been $4,930,636; done on equipment, $481,169.

Q. That is, you are referring in giving the figures to Exhibits 268 and 269 introduced by Mr. Thompson?

A. Yes, sir.

Q. They appear on those papers?

A. Yes, sir.

Q. Now, give us the general condition of this property or any principal changes, improvements, that have been made under the present general condition both for roadway and equipment.

A. As to roadway the property is in splendid condition. There still remains, of course, the normal program of rail renewals that will continue—should continue each year as the railroad is operated. Our ballast program is very well up to date and our maintenance of way deferment, if
[fol. 1167] there was any, has been entirely picked up. The railroad is, in my opinion, in very good shape. As to maintenance of equipment, any deferment that may have existed on our power has been picked up. There still exists, in the opinion of our mechanical officer, some deferment on cars. Approximately half of that deferment will be picked up this year and that will leave approximately $750,000 which we expect to pick up in 1942 and 1943.

In the process of this program we will have eliminated approximately 2,500 units of equipment, equipment which,

by reason of our business, is no longer needed and we are not replacing. In replacing units, however, we are increasing the capacity of those units so that we will still have, from the standpoint of cubical capacity or carrying capacity approximately the same amount of equipment that we started out with in 1938 when we made our equipment survey. The railroad is well equipped now as to yards. We have in mind five additional small Diesel switchers which we probably will purchase within the next year or so, but if our experience follows the other railroads those, of course, will pay for themselves in the savings that we are able to accomplish.

We will need 500 boxcars some time between now and 1945. Those boxcars will be needed to replace older equipment, and it is entirely possible that we may decide to take advantage of the opening that we have now to purchase [fol. 1168] them because if we do we can make some saving in our maintenance of equipment by discontinuing some heavy maintenance on cars that we have been keeping in service.

So far as our road equipment, road power, is concerned, I don't believe that we will need any additional road power for some time unless we have a much bigger increase of business than we can now forsee. We will have, after this year, completed all of the signalling of our main line with the exception of the Denver-Pueblo territory where we have got a double track railroad and probably won't signal for a good many years, and a little piece of territory between Ogden and Salt Lake. We still have some territory between Grand Junction and Dotsero where we are equipping the C. T. C. and where we have a program that will take us a couple of years more to tie together the two pieces.

Q. That C. T. C. greatly increases the capacity of the line: doesn't it?

A. Very much so, yes, sir.

Q. What percentage, would you say?

A. My own opinion is that track equipped with proper passing tracks and centralized traffic control has about one hundred—well, about 70 per cent of capacity of double track. In other words, I think——

Q. In other words, it is equivalent to 70 per cent to what you have carried for double track?

[fol. 1169] A. Yes, sir.

Q. Additional business?

A. Yes, sir.

Q. Now, going back for a minute before you go on, the equipment that you spoke of as being on order costing approximately $4,000,000 for this year is not included in those statements, 268, and 269 to which you referred; is it?

A. No, sir.

Q. That equipment is in addition to the expenditures that have been set forth in statements 268 and 269?

A. That is correct.

Q. Which would bring it up to something around 21,000,000 if that were included?

A. Yes, sir.

Q. And that is all charged to capital, of course, as new equipment?

A. That is true.

Q. And issued as you have stated.

Now, you spoke of accelerating the improvment of certain older cars. Would you make that a little clearer and, if you can say so, what it will increase the expense in 1940 over what the regular schedule which runs over a number of years would be?

A. Well, we had 1,447 boxcars, 40,000—or 40-ton capacity, 40-foot cars in our series 66,000, 67,000. Our plan [fol. 1170] our equipment forecast indicated that those cars would probably start taking themselves out of service, from an economic standpoint, about 1950 to 1952 or 3. Our older cars are 40-ton 36-foot cars and are much older, and they were costing a great deal of money to maintain. They are taking themselves out of service pretty rapidly now. Rather than buy new cars to put in coal or concentrate bullion and rough trade, we took our 66,000 and 67,000 series cars which up to that time had been our Class A cars and worked out a program of strengthening them to throw them into the so called rough trade, and it is costing about $405 a car.

We had planned to do that over a period of four to five years but further decided, in view of the situation and the demand for equipment, that we should expedite that program, and that calls for an expenditure of approximately $580,000.

Q. Which you had not contemplated spending——

A. We had contemplated, say, a fifth of that this year, Mr. Anderson, about $125,000 this year, so that we are

throwing into 1941 $400,000 to $450,000 deferment that we expected to make up in '42, '43 and '44 and '45.

Q. I see. And that additional expense is carried into your forecast for this year which Mr. Thompson has testified to?

A. Yes, sir.

Q. And affects your earning statements accordingly?

A. That is correct.

[fol. 1171] Q. Now, is it not a fact that your present ownership of the cars—you have spoken of power as being adequate for the future needs—is equal to or in excess of the total ownership of cars in the country established by the AAR in its formula, regardless whether the formula is good or bad that is a fact; isn't it?

A. That is a fact. If you take the formula and correct it to this extent, they left off a few little items, and then they had a 6 per cent bad order, and our bad order has been less than 3 per cent for some time so, giving that consideration, we have an excess ownership according to their formula, whether it is good or bad.

Q. Of the proportion of cars that should be allotted to each railroad in the United States?

A. That is correct.

Q. Mr. Bradford, you have said that, so far as roadway and structures are concerned, your property is now in good condition. I take it from that that your improvement program, so far as roadway and structures are concerned is about completed. Am I right on that?

A. The big items. We will continue, of course, to have each year an improvement program and maintenance of way and structures.

Q. Of course.

A. We will have 60 miles of rail each year; we will have [fol. 1172] bridges and things like that, but our 1941 forecast of our 1940 expenditure, for that matter, somewhere around those items, can be taken for our future maintenance of way and structure, sir.

Q. In other words, you regard the program set up by the trustees at the beginning of the trusteeship in 1938 for extraordinary improvements, if I may call it that, as completed and you now have your normal A & B expenditures as every railroad has; is that right?

A. That is right, so far as maintenance of way and equipment is concerned.

Q. So far as your equipment is concerned, when you have acquired these new additional engines and cars which you have indicated, your equipment, not only by the AAR standard, but in your opinion also is adequate now? Isn't that the situation when you finish these 1,400 cars?

A. As I stated, some time between now and the next two or three years we ought to buy 500 additional boxcars. We also between now and the next three or four years will probably buy 500 additional coal cars which will take the place of about 1,100 miscellaneous coal cars, but if our figures are correct as to the cost of maintaining those 1,100 cars, the 500 additional boxcars can be adequately serviced by the saving that we will make in maintenance of equipment expenditures.

[fol. 1173] Q. Yes. And your equipment depreciation is now in excess of your equipment maturities?

A. Yes, sir.

Q. And your depreciation on this additional equipment, if you bought it, would provide for the necessary equipment maturities, generally speaking?

If you bought the additional equipment you mentioned, the savings which you would effect in the future would substantially take care of the additional capital charge there involved, the equipment having been bought on equipment trust?

A. Yes, but we are trying to purchase this new equipment on this basis: You must cut your maintenance expenditures enough to pay for these new cars.

Q. In other words, retiring those old cars and buying new cars would pay for the new cars?

A. Yes.

Q. Now, taking that railroad in that shape, the fine shape which you have indicated, have you been able to accelerate your schedules and improve your operating conditions to a material extent and, if so, will you indicate to the Examiner generally the result of those expenditures?

A. Well, there has been, of course, material improvement and acceleration of schedules in the past number of years, and by reason of these improvements it is easier for us to meet the competitive schedules now than it was some years [fol. 1174] ago. That has resulted from improvements to roadway and structures and also from this new power that we have been purchasing. We have a railroad now that is capable of taking care of a great deal of business, taking

care of it adequately. I can't tell you how much more or I can't tell you what directions it might come from or in what months, but I do know from my own practical knowledge of the railroad that we could take care of a great deal of business and much better than we could have taken care of it 5 or 6 years ago.

Q. Now, let me ask you a few specific questions. To start with, with your improvement in your track structure and your rail, ballast, heavier rail and other things that are shown in the annual reports—you need not go into detail—you have better operating conditions, so far as your physical structure is concerned; haven't you?

A. Yes, sir.

Q. And with train control, traffic control, and other improvements such as signalling, and so forth, you can operate your trains at higher speed, both freight and passenger; can't you?

A. That is correct.

Q. And you are doing that?

A. Yes, sir.

Q. You also with your new equipment, which is a higher capacity, an improved structure, as all new equipment is [fol. 1175] over old equipment, you can make better schedules, carry more business, with less units of equipment; can't you?

A. Yes, sir.

Q. Therefore, the entire operating condition which confronts the railroad today, from your view, as I take it, is very superior to what it was in 1937, for instance; is that correct?

A. That is correct, and that it will be further improved when we get this equipment that is now on order.

Q. Get what is now on order?

A. Yes.

Q. The necessary result of that is that it makes a permanent improvement in unit cost of handling the business, assuming that the general cost, labor, and so forth remains the same; doesn't it?

A. Yes, sir, it will, if we can hold what we have, which should be something.

Q. Now, you spent, according to your statement—will have spent, outside of charge to operating expenses through betterments, you will have spent, including this year, some-

thing over $24,000,000 on this property since 1935, November 1st? I will ask you whether, in your opinion and your familiarity with properties, the improvement in operating conditions, the deduction of expense and other benefits accruing from those expenditures, will provide a good return [fol. 1176] upon the investment which you have made in them?

A. Well, that is a pretty difficult question to ask because a lot of this stuff can be——

Q. If you can't answer it, then why did you make the expenditures?

A. We have to make some expenditures from the standpoint of safety. Now, it depends entirely upon how you want to capitalize safety.

Exam. Boyden: You have to make expenditures to keep up with the trend of the times and to handle the traffic you now handle; don't you?

The Witness: That is right, and we have to make some expenditures to comply with rules and regulations of law, some of which we do not agree with, but the biggest expenditure made on our railroad was for power, and the power will pay for itself. The cars, to a certain extent, will pay for themselves, I mean will return to us in savings in cost a certain amount of their cost.

For example, these 500 boxcars we are considering now have a protection, not as a return, but we will get $60,000 a year by return in reduction of cost of maintaining older cars that they will take the place of. Now, we can maintain the older cars through operating expenses and take care of the same amount of business, but I can't tell you that this $17,000,000 odd actually made us a return because [fol. 1177] so much of it is hard to put down, from a standpoint of saving. I know that good ballasted track will reflect a credit back to your maintenance expense. I can't tell you how much.

Q. No, you can't, but you can approximate the savings that result from ballast in maintenance expenditures. You have got, say, to equip your roadway with tools; haven't you?

A. Yes, sir.

Q. And they are very economical; are they not?

A. Yes, sir. I think that we are getting the effect of that economy in our maintenance of way. I would say this,

from a practical standpoint, that you take 1940, the performance of 1940 will be somewhat—should be somewhat improved in the coming year.

Q. What would you say your maintenance of way will be in the coming years, looking ahead?

A. Well, if we have somewhere between twenty-five and twenty-eight million, our maintenance of way should be around three million, $3,200,000. Our maintenance of equipment expenditures have been estimated normally, after we take care of this deferment at—excluding depreciation, say, $4,188,000. Now, you have got to add from $1,400,000 up for your depreciation, depending upon what you have.

Q. Yes, but that isn't an expense in the usual sense. You pay off capital.

A. Well, it charges in our operating expense for that. [fol. 1178] Q. Yes.

A. Then we will always have some operating expenses in connection with improvements and retirements, so that I will say if you take on that situation—and this ought to come after 1943—that you have $4,100,000 or $4,200,000 ordinary maintenance to which you would add your depreciation which, at that time, will probably be a million dollars four and a quarter and, say, $50,000 to $100,000 for operating expense in connection with additions and betterments.

Q. That is on equipment?

A. On equipment, yes, sir. Our transportation ratio depends a great deal on when we get the business, where we get it, our expenses, and labor. I think our transportation ratio for 1940 was a pretty good check. There was nothing in maintenance of way and nothing in maintenance of equipment that will add much to that for succeeding years.

Q. And I believe you have said already—if you haven't, I want to make it clear—that these improvements and when you get the equipment you have ordered, develop the capacity of your properties to handle business, additional business will be very greatly increased; am I right in that?

A. Yes, sir.

Q. You say that so far as your central traffic control is concerned, you say that increases the capacity of the track, in your judgment, about 70 per cent and that the other [fol. 1179] facilities which have been provided and new power which has been provided greatly increase the capacity

of the property to handle increased business and to handle it at better speeds and at lower costs, unit costs. Am I right in that summary?

A. That is correct, sir.

. . . . . .

[fol. 1180] WITNESS R. K. BRADFORD.

A. I think that the exhibits that are made up by Mr. Thompson, as I stated, are mathematically correct. As to the value of them, they might be considered more valuable to one person than they would be to another. I think it is as good a horseback estimate as you can make of what happened in 1940 and what might have happened in previous years had the same conditions existed in previous years as existed in 1940.

Q. Did the same conditions exist in previous years as they did in 1940?

A. By his mathematics he has made the same conditions exist in previous years, to a large extent. You can't mathematically fool with the weather or anything like that.

Q. Let us examine that. Do you think 1940 was a good year to take as a test year or to compare the unit costs of these two railroads?

A. 1940 was the best year up to that time from the start of the trusteeship.

Q. Best year for what?

A. Best year for the railroad.

Exam. Boyden: Best year for the results of the railroad?

By Mr. Clay:

Q. You mean for the Denver & Rio Grande Western?

[fol. 1181] A. Yes; that is what I am talking about.

Q. But not the best year for the Denver & Salt Lake?

A. Oh, no, not the best year for the Denver & Salt Lake, but the question that Mr. Thompson was asked was to take the costs in 1940 that resulted from the various expenditures made by the trustees in their procurement programs and to project them back over the previous years to determine what may have happened during the previous years, had those adjustments been in effect during the previous years.

I think that gives you a pretty fair estimate of what might have happened.

Q. Mr. Thompson introduced as Exhibit 260 the annual report of the Denver & Rio Grande Western for the year 1940. I turn to page 11 of that exhibit and ask you to look at the figures on that page and tell me whether the maintenance of way and structures in 1940 was greater or less than in 1939.

A. Maintenance of way and structures was less than in 1939.

Q. By how much, roughly?

A. $290,049.33.

Q. Now, how about the other maintenance item there just below that?

A. Maintenance of equipment was less than in 1939 by $27,771.31.

Q. So 1940 certainly was a better year to take, wasn't it, [fol. 1182] in the case of the Denver & Rio Grande Western than 1939?

A. Yes; I said it was the best year in the last five or six years to take.

Q. I agree with you, but now look at Exhibit 261 at page 10. I will ask you to look at the figures on that page and read me the maintenance of way and structures figures, the maintenance of equipment figures for '40 and '39, respectively, in the case of the Denver & Salt Lake.

A. Maintenance of way and structures was $381,807.92; or an increase of $32,203. Maintenance of equipment was $531,289.30, or an increase of $42,098.72.

Q. All right. Now, am I right in saying that in 1940 these maintenance items were less than in 1939 on the Denver & Rio Grande Western but more than in 1939 on the Denver & Salt Lake?

A. That is correct.

Q. Now, if you will turn to page 15 of the same exhibit, you will see a column headed "Retirements and Adjustments" on the Denver & Salt Lake. Weren't those larger retirements and adjustments in connection with the main line, that is, the Dotsero cut-off line?

A. I don't know, Mr. Clay. I haven't in mind or available the breakdown of those returns and adjustments.

Q. Well, you testified on power, the increases in power equipment this morning. Did I understand you correctly to [fol. 1183] say that the heavier power on the through route over the cut-off was put into operation in the fall of '39?

A. The heavier power over the cut-off—that is, the heavier Rio Grande power—when we opened up over there we opened up with Mallet Power, but the heaviest Mallet Power that we owned was put over there in the spring of '39.

Q. The spring of '39?

A. Yes.

Q. Now, was it possible to use that heavier power over the Dotsero cut-off efficiently without doing considerable track alignments and track improvements?

A. The work necessary for the heavier power on the Denver & Salt Lake consisted of some new rail and some ballast and some bridge strengthening.

Q. So a heavier power could be used——

A. That is correct.

Q. —on that line?

Now, that heavier power was power owned, bought and used by the Denver & Rio Grande Western; wasn't it?

A. Yes, sir.

Q. If the Dotsero cut-off had never been built it would never have been necessary, unless the Denver & Salt Lake bought locomotives similarly heavy, to have spent that money, would it, on the track alignments?

A. Depends on what you consider necessary. I, per- [fol. 1184] sonally, consider that the Denver & Salt Lake, regardless of the Denver & Rio Grande's interest, might have made some money by putting their track in a little better shape over there so that they themselves with their heavy power could have moved better.

Q. They did make money under the Freemen management?

A. Yes, they made some money.

Q. And the cutoff, I believe, was opened in '34; was it not.

A. Yes; '34 is right. June 15.

Q. And all the money which has been spent by the Denver & Salt Lake management on the improvement program has been on that through route; hasn't it?

A. No, sir.

Q. Well, the——

A. There has been considerable money spent west of Orestod in the way of laying rail, some ballast, some ditching, some line revisions, small ones, building up rail ends, ties, bridges.

Q. Just take the year 1940. You heard Mr. Thompson testify that there was about $200,000 spent on, I think it was, automatic train control, was it? Telephones?

A. No.

Q. What was it?

A. In the year 1940 on the Denver & Salt Lake there was about $339,000 spent on additions and betterments.

[fol. 1185] Q. Yes, sir.

A. The two big items in that year were automatic block signals and a new coaling station and layout at Sulphur. The complete program as to block signals on the Denver & Salt Lake will approximate $200,000, but some of that slopped over or worked over into '41.

Q. Well, all the block signals were put on the main route, weren't they, the cut-off?

A. The block signals were put between Denver—between Prospect and Denver and West Portal.

Q. The coaling station was on the main route; wasn't it?

A. Yes, sir; Sulphur.

Q. Now, when this block signaling project is complete, won't the Dotsero cut-off route be completely block-signaled from Denver to Bond?

A. The cut-off will be block signaled this year from Dotsero to Orestod, and that will leave the territory from West Portal to Orestod, a distance of approximately 60—about 69 miles yet to be signaled.

Q. But all the rest will be block-signaled?

A. The territory is now block-signaled between Fox Junction and Denver and West Portal, and the cut-off between Dotsero and Orestod will be signaled this year.

Q. Of course, these expenses have been reflected in the Denver & Salt Lake but they have contributed very sub-

[fol. 1186] stantially in the reduction of the unit cost of the Denver & Rio Grande Western?

A. The block signals reflect very little in the operating expenditures of the Denver & Salt Lake because primarily they are road and equipment, that is, they are capital charges, and the contribution to the economical operation from block signals is a question of opinion, somewhat questionable. I think it makes a very much safer railroad, and I have always felt that you get a little faster movement in a railroad like that, particularly that is protected by block signals, because the men feel safer, but I would hate to put down in money what block signaling saves you.

Q. The track alignments plus the block signals and the other improvements have certainly increased the transportation of the line; haven't they?

A. Yes, sir; materially.

Q. And enabled a larger portion of bridge traffic to be hauled over the Denver & Rio Grande Western over the cut-off route?

A. Yes; the Denver & Rio Grande Western handles a great deal of bridge traffic over there.

Q. Isn't it true that the unit cost for the bridge traffic of the Denver & Rio Grande Western is less than the unit cost for the non-through traffic, by reason of the improvement on the main line, the $20,000,000 which has been spent [fol. 1187] largely in heavier power there on the main routes?

A. That the unit cost on the main line is less than the unit cost on the non-main line?

Q. On the system.

A. Yes; that is correct. The unit cost for the main line is less than the unit cost for the system.

Q. And it would seem obvious, wouldn't it, Mr. Bradford, that this money that the Denver & Salt Lake has spent in improving its main line has, therefore, contributed to the reduction in the unit cost of the Denver & Rio Grande operation with respect to the through traffic?

A. Yes, I think there has been some contribution in that expense.

Q. Now, do you know what Mr. Thompson's two exhibits were introduced to prove or what was the purpose of introducing them?

A. What two exhibits?

Q. The exhibits 262 and 263 which restate the costs for '36 to '39, inclusive, on the basis of the unit cost for 1940.

A. No, I don't know what they had in mind proving by them when they asked us to make them up, no, sir.

Q. Now, I am going to ask you a few more questions to develop whether they can be depended on to prove anything. I hand you an exhibit, No. 260, page 24, and refer you to the figures for 1940 for freight and passenger train miles, [fol. 1188] the passenger train miles being 2,000,000 some odd miles and the freight train miles three and a half million. By merely using a pencil, I think you will find that the passenger miles will approximate 20/55 of the total of

passenger and freight train miles, or, in other words, 4/11 of the total train miles, which is approximately 36½ per cent of the total train miles which are passenger. If you will bear that figure in mind a moment, and then turn to Exhibit 261 which shows the train miles for the Denver & Salt Lake, will you look at the figures under 1940 and tell me whether it is approximately correct to say that about 30 per cent of the total of the train miles is passenger——

A. What page is that, Mr. ——

Q. That is page 22.

—is passenger train miles in the case of the Denver & Salt Lake? That is, you break down the mixed train miles.

A. The figures show this: That freight train miles on the Denver & Salt Lake are 211,000. Mixed train miles, 168,000. Passenger train miles, 171,000.

Q. Well, we wouldn't be far wrong, would we, if, by breaking down the mixed train miles, we venture to say that perhaps 50 per cent of the mileage in the case of the Denver & Salt Lake is passenger miles?

A. Yes, I think you would, Mr. Clay.

Q. What would you say it would be?

[fol. 1189] A. That would mean that you have to breakdown the mixed train mileage and charge about 65 per cent altogether to passenger.

Q. Would you say 45 per cent would be nearer?

A. No, so far as passenger is concerned on the mixed train, it is more or less incidental. Mixed train was primarily put on to handle overnight merchandise and so called fast business on the Denver & Salt Lake that was giving way to trucks.

Now, incidentally, they stuck on the hind end a baggage car and a combination coach with four sections on it for a little sleeping service, but the revenue for the passenger train is pretty light.

Q. I am not talking about passenger revenue. I am talking about passenger miles.

A. That is some way to split mileage with some relation to what the passenger is put on for.

Q. What would you say? Would you say 45 per cent instead of 50 per cent?

A. No. From the work that is being done, I would say that about 90 per cent of it ought to be charged to freight and about 10 per cent to passenger.

Q. Let us see if they do that. 10 per cent of the 178,000 would be, roughly, 17,000, wouldn't it, and that 17,000 would be added to the 171,000, which would produce 188,000. Would you take your pencil and see what percentage [fol. 1190] 188,000 is of the total train miles?

A. About 30.

Q. Your estimate, without figuring it out, would be around 30 per cent?

A. Yes, sir.

Q. Now, to come back to this formula of the Commission's for segregating freight and passenger expense, wasn't that really—does it afford a basis of comparing the freight and passenger on the same railroad as between different years? Would you agree with my statement?

A. Why, if you take the different years and split them up on the same arbitrary basis, yes, sir, it would give you a comparison on the same railroad.

Q. It is a basis of comparison as between different years on the same railroad?

A. That is right.

Q. But would you say it affords a basis of comparison as between the same year on different railroads?

A. No, sir, I would not, because there is so much that you have got to know about any passenger service on any railroad that you can't compare passenger revenue or passenger train miles on railroad A with that on railroad B by any formula such as that.

The Denver & Salt Lake has got one straight passenger train a day which runs from Denver to Craig and back. It [fol. 1191] performs a necessary service. It is not kept on there because it is making anybody a lot of money. It is just swapping dollars.

Q. Now, it is, of course, true, isn't it, that the less the proportion of total expense that you assign to passenger expense, the greater will be the unit cost for freight expense?

A. That is correct, if you take the arbitrary division between freight and passenger and reduce that to passenger you will have an increased charge toward your freight.

Q. And, conversely, the greater the proportion of total expense which you assign to passenger expense the lower will be your unit cost for freight expense?

A. Correct.

Q. Well, let us see how that works out in the case of these two railroads. I hand you Exhibits 262 and 263. Look at the year 1940 alone. Is it not, roughly, true that on this exhibit one-fifth of the cost of—one-fifth of the total expense is assigned to passenger expense?

A. That is about right, yes, sir, on the D. & R. G.

Q. Yes.

A. Yes.

Q. I believe you stated I was approximately correct in my statement a while ago, based on figures on page 24 of Exhibit 260, that 36½ per cent of the passenger miles of the Denver & Rio Grande Western—no; 36½ per cent of the [fol. 1192] total miles are passenger miles?

A. That is correct.

Q. So that in the case of the Denver & Rio Grande Western you assign to 36½ per cent of the total mileage one-fifth of the cost?

A. Under that method of figuring, yes, sir.

Q. Now, in the case of the Denver & Salt Lake, which is shown on Exhibit 263, roughly, what percentage of the total expense is assigned to passenger expense for the year 1940?

A. About 15.

Q. The passenger operating expense is $232,000; isn't it?

A. That is right.

Q. And the freight operating expense is three million——

A. No.

Q. Is one million, five?

A. The total is $1,782,000.

Q. About one-seventh; isn't it?

A. About 15 per cent.

Q. You would say 15 per cent?

A. Yes, sir.

Q. In other words, Exhibit 263 assigns 15 per cent of the total expense to passenger expense, though, as you testified a while ago, 30 per cent of the total mileage of the Denver & Salt Lake is passenger mileage?

A. That is correct.

[fol. 1193] Q. Now, on the basis of those figures is there any real basis of comparison between the way the freight and passenger expense is allocated on Exhibit 262 and the way it is allocated on Exhibit 263?

A. Not on your theory, but your theory, Mr. Clay, would mean that a passenger mile and a freight mile cost the same, so that the expense ought to fall in proportion to

the mileage, and that isn't at all correct. The freight miles cost more mile for mile than your passenger in direct operating expenses.

Q. I certainly didn't mean that.

A. So you can't take any of those figures and split them on a mileage basis and say, because it is 50 per cent passenger and 50 per cent freight, that the expenses ought to be split fifty-fifty, because it won't work that way. Wages are higher; fuel is higher on freight than it is passenger.

Q. Well, I am not interested so much in illustration as in the correctness of the principle.

A. Regardless of what I may think of how those schedules are made, I think that exhibit was made up with a great deal more care and with more thought of getting a proper proportion than we have got here just bantering these train miles back and forth between ourselves. I may not agree with some of the Commission's allocations, but——

Q. You testified you didn't agree that you thought it was [fol. 1194] arbitrary.

A. I didn't mean "arbitrary" in the way you considered it.

Q. That is the method used.

A. I say "arbitrary" because there is an arbitrary division between freight and passenger, an arbitrary expense not with relation to certain work, for example, but with regard to certain stations. They charge 25 per cent passenger and 75 per cent freight. Now, naturally, you couldn't go through every station and make a study of it to see exactly what proportion is chargeable to each.

When I used the word "arbitrary" that is what I meant. I didn't mean to the extent that they had made their division without any thought and just jumped out on the end of the plank and said, "Here it is."

Q. Now, I think you figured on the basis of Exhibit 263 fifteen per cent of the total expense was charged to passenger business.

A. Yes, sir.

Q. Don't you think that is low for the Denver & Salt Lake?

A. No. As a matter of fact, I think it is high, because I approach a train and a situation on the Denver & Salt Lake in this way: We have charged to that passenger train $232,781. Now, if we took off the passenger train, how

much could we save? We know that we would lose so much passenger, so much mail and a little amount of express. [fol. 1195] If we took off the passenger train we certainly couldn't save $232,781, because I figured it out. We could save about 62 cents a train mile by taking off that expense, and we are getting in about 63 or 64.

Now, that doesn't compensate you for any of the wear, if you please; of your plant, but to that extent on the Denver & Salt Lake I think we are charging too much to passenger. I think we are on the Denver & Rio Grande, but that is only my opinion. They are both made exactly in accordance with formulas that have been worked out over a number of years. In my opinion of that, we charge too much to passenger and not enough for freight.

Mr. Anderson: In accordance with the formula in use for a number of years, you mean the ICC formula?

The Witness: Yes.

Mr. Anderson: All right.

By Mr. Clay:

Q. Now, are you testifying as to the power that the Denver & Rio Grande Western has?

A. Yes, sir.

Q. With that existing power, of course, you estimate you can handle the amount of business you are now handling?

A. Yes, sir.

Q. What do you estimate will be the gross business of the Denver & Rio Grande Western for 1941?

A. $28,000,000.

[fol. 1196] Q. $28,000,000?

A. Yes, sir.

Q. Now, if, due to the expansion of the defense program, it should get up thirty million, do you think you could handle it with the present power without increasing the operating costs?

A. No, sir.

Q. Your would have to bring out into operation a lot of these old style locomotives; wouldn't you?

A. Any increased business will increase your operating costs unless you are pretty lucky getting somewhere where you have got a half train or something like that. It doesn't work that way.

Q. What was your gross in 1940?

A. $26,200,000, approximately.

Q. And you estimated gross in 1941 of——

A. $28,000,000.

Q. —$28,000,000?

A. Yes, sir.

Q. Do you think you can handle the $28,000,000 this year on as low a unit cost as your $26,200,000 in 1940?

A. Yes, sir.

Q. But you couldn't handle thirty million on the same unit cost, on as low a unit cost, as you handled the $26,200,000 in 1940?

[fol. 1197] A. I would say that, coming in the proportions in the same months in the same directions and the same bad breaks that we always get, that if we got $30,000,000 this year with our present power, that we would have to put some of our smaller engines on the main line and there might be a slight increase in our transportation cost unit.

Q. Now, what was the gross on the Salt Lake in 1940?

A. $2,363,000.

Q. What do you estimate will be the gross in 1941?

A. Have you got that forecast here handy? I can dig it out. I don't remember it. $2,255,000, approximately the same.

Q. Now, would you say that you could handle a three million gross on the Salt Lake with the present power and coming at the same periods and moving in the same directions, without increasing the unit cost?

A. I think we could. We handled $2,856,000 in 1936 on the Denver & Salt Lake and another $140,000 spread over the peak months. I don't believe it bothered us particularly.

Q. I believe Mr. Thompson testified that the Salt Lake could handle four million gross without increasing the unit costs. Do you agree with that?

A. I did not understand his testimony that way. No, I don't. I don't believe the Salt Lake could handle four million gross with their present power without increasing their cost, unless it all was westbound. Where they are now [fol. 1198] hauling empties, if they could get the gross in that direction they could do a great job, but chances are it will be all eastbound if they get it.

Q. Isn't most of the oil shipped on the Salt Lake all westbound?

A. No, sir; it is all eastbound.

Q. All eastbound?

A. Yes, sir.

Q. You mean right at the present moment it is eastbound?

A. It is all eastbound. There are no shipments on the Salt Lake except between Denver and Craig and Orestod. When the crude oil is moving it moves over the Denver & Rio Grande Western from Denver and Orestod and then moves east over the Salt Lake.

Q. What is it, eastbound to Bond?

A. Eastbound to Orestod and westbound from Orestod.

Q. Yes.

A. The oil comes in the same direction as their loaded coal. All their business is eastbound.

Q. Well, I think we are probably talking about the same thing but expressing it differently. The oil does move to Utah, doesn't it, the petroleum oil?

A. Yes, but it moves eastbound over the Denver & Salt Lake, which is in the same direction as their eastbound coal movement. My statement was that if the Salt Lake could [fol. 1199] get lucky and handle business westbound they could handle four million or four and a half million and not only not increase their unit cost but decrease it materially, because they would get a balanced business, but they handle nothing westbound, practically speaking, except empties, and all their loaded is eastbound.

Q. I see. Well, what would you say would be the largest amount of gross that the Salt Lake could handle without increasing the 1940 unit cost?

A. That would be just a guess. The unit costs——

Q. Three and a half million?

A. The unit costs in 1940 will go down some, in my opinion, up to about two million eight to three, and from three on, because they would be running out of power, why, then, they would start having the unit costs go up because they would throw back into service a lot of small power and they would have to put on a lot of equipment or additional power if they are to keep the traffic moving.

Q. To the same extent as the Denver & Rio Grande Western?

A. To a greater extent than the Denver & Rio Grande Western.

Mr. Anderson: You have got full orders, haven't you, Mr. Anderson?

The Witness: Right now, I am talking about. Yes, we are in good shape, but right now I am talking about.

Mr. Clay: That is all I have.

[fol. 1200] Exam. Boyden: Any further cross-examination?

Redirect examination.

By Mr. Anderson:

Q. Mr. Bradford, there i sa question of power. Mr. Clay asked you if, with your present power, there would not be an increased cost of $30,000,000. You said there might be. Now, you have already ordered and have now in process of delivery or promised delivery this year additional power which you described this morning; haven't you?

A. Yes, sir.

Q. Costing approximately $4,000,000?

A. That is correct.

Q. Including 15 Diesel switch engines and three, I think it was, heavy 5,400 horsepower road Diesel engines for freight service; have you not?

A. Yes, sir.

Q. Now, with that new power can't you really handle the business that you are handling now, tonnage, at a lower unit cost, for instance, with Diesels than you can do it with this other stuff?

A. Yes, sir.

Q. You can reduce your unit cost?

A. Yes, sir.

Q. And with that additional power in service you could handle thirty millions or very considerably over thirty millions without any increased unit costs; couldn't you?

[fol. 1201] A. I think so, yes.

Q. As a matter of fact, can you see in prospective any business that the Denver & Rio Grande could not handle with its present power plus this new power of an improved character, plus central traffic control and other improvements you have made at a continually decreasing cost, unit cost?

A. I wouldn't use the words "continually decreasing," because we are going to run out of slack some time, but certainly with our new power and with our improvements we can handle increased business, and for the first few points

of increase at least we will get a decreased cost. In other words, we will have more power after this new power is delivered. We will have some surplus high class power.

Q. You will have more efficient power.

A. Yes, sir.

For example, at the present time we are making about—I will show you the—we are making—in the year 1940 we made 30.39 per cent of our locomotive miles with Mallet. That is our most efficient engine. In 1939 we made 29.8. Going back to 1936, we made only 18 per cent with Mallets. Now, the additional Mallets we are buying, plus the additional big Diesels, will further retire from operation some of this smaller power and, naturally, we expect to get a decreased unit cost with it. That is the only reason that we are buying it.

[fol. 1202] Q. And the Diesels, according to the testimony, on the Santa Fe and other roads indicate a very decided efficiency and reduced cost, do they not?

A. Yes, sir.

Q. Therefore, you can handle your business more efficiently and more economically with your power now at hand and within any reasonable limits of increase; can't you?

A. Yes, sir, I think so.

Q. Now, you were asked about the question of the ICC formula. Not being an accountant, I wouldn't imagine you would want to testify on the ICC formula, but at the same time, as you understand, those exhibits that have been a matter of discussion here were made up in strict accordance with the ICC formula; were they not?

A. Yes, sir, I understand.

Q. Now, the ICC formula, as I understand, distributes first the cost directly attributable to passenger and allied services to passenger and allied services; is that true?

A. That is my understanding.

Q. And the cost directly attributable to freight services to freight services?

A. Yes, sir.

Q. And then the common cost in between which they distribute on a basis determined by the ICC to be approximately correct or be reasonably near as they can make it, they [fol. 1203] distribute it between passenger and freight; isn't that true?

A. That is correct.

Q. And the distribution has been made in accordance with that formula here of that different cost. But, of course, you can't make an actual absolute distribution, for instance, of superintendence; can you?

A. No, sir.

Q. And you say even if you cut off the business the chances are you can't get rid of any superintendence; can you?

A. No, sir.

Q. And if you cut it off you can't make an absolute and mathematical distribution of maintenance where passenger and freight trains run on the same road; can you?

A. No, sir.

Q. Therefore, you take the formula that the ICC has developed as the best available and you make the distribution on that basis, don't you, when you make up these figures?

A. Yes, sir; that is the way those figures were made.

Q. You were asked something about the use of the year 1940 of unit costs and these were—the year 1940 was used, was it not, for the purpose of—no; put it this way: Was used as being the last year available in which the results or benefits derived from the improvements made on these properties show their largest manifestation? Isn't that about the way it was?

[fol. 1204] A. Yes; that is the reason I assumed that 1940 was used; yes, sir.

Q. In other words, you couldn't have gotten the benefit of these improvements as completely in 1939 or '38 as you did in '40 because many improvements were made in '38 or '39?

A. We were told to take the last available year, so that was the last available year.

Q. So naturally that showed greater improvements than had been made up to that time; didn't it?

A. Yes, sir.

Q. Now, you were asked if that would apply to the Denver & Rio Grande Western and the Denver & Salt Lake. Both of them were improved up to 1940 and improvements are continuing; aren't they?

A. Yes, sir.

Q. In other words, improvement of the track on which the Denver & Rio Grande Western operates over the D. & S. L. benefits, to the extent that the D. & S. L. trains are moved

over that track, the separate operation of the D. & S. L. also; doesn't it?

A. Yes, sir.

Q. Of course.

Now, can you think of any better year to have used to show the results; as far as you could do it, of these improvements and betterments either on the D. & S. L. or the [fol. 1205] D. & R. G. W.?

A. No. If the intent of that statement was to show the benefits of the improvements that were made in the previous years, of course, we should do just what we were told to do, and that is take the last year available in which improvements were made.

Q. On both railroads?

A. On both railroads; that is right.

Q. If you want to take statements of that kind can you think of any better way to do it than use the same year for both roads? If so, I would like to know it.

A. No; I think the only way you can do it is use the same year for both roads. Otherwise you will get into difficulty, because we have been getting a swing from year to year, particularly on the Denver & Salt Lake.

Q. You have a swing on all railroads; don't you?

A. Yes, sir, but the Denver & Salt Lake, their operation and their revenue is a pretty good thermometer.

Q. Of what?

A. Of weather conditions and things like that. In other words, if the Denevr & Salt Lake thermometer goes up you can figure you have had a heavy winter, and vice versa.

Q. What kind of a winter did you have in 1939 and 1940?

A. The spring of 1940 was pretty severe and we sold a lot of coal. 1941 was pretty mild.

[fol. 1206] Q. 1940 was a fairly tough year; wasn't it?

A. Fairly tough spring out there and a pretty good fall.

Q. Now, I ask you, is it not a fact that your reported earning statements during these years of improvement by the trustees are materially distorted by extraordinary maintenance and other charges which, I think, one year went up as high as 46 per cent of your gross revenue? That would be necessary during an improvement program; would it not?

A. Yes, sir. Our reported earnings during that period carry a considerable charge as a result of our improvement program.

Q. The reported net, for instance, is not any indication unless adjusted in the earnings of the road?

A. I think that is a fair statement.

Q. In other words, taking your unit costs after the improvements are finished in 1940 and carrying it back over those years, as well as carrying it forward for a prospective basis is a better approximation of the earning power of the properties than to take a distorted statement taken from the reported earnings of the companies; isn't that true?

A. I think so.

* * * * * * *

[fol. 1207] STIPULATION AS TO RECORD

Mr. Marsh: May I ask are the installments of the printed record still pouring into this record?

Exam. Boyden: Mr. Marsh, I think probably before the close of this hearing we will try to get a stipulation with respect to that and make it clear. As a matter of fact, we might as well do that now while the question is before us to save going back to it.

Are counsel willing to stipulate that the Commission may consider, as a part of this record, all of the court papers transmitted to the Commission by the Clerk of the Court to file in the docket?

Mr. Clay: Perfectly satisfactory to us.

Mr. Marsh: Satisfactory to us.

Exam. Boyden: Is there any objection? And when I say "all the court papers" I intend the stipulation to cover papers that are sent to the Commission and filed in the docket after the close of the hearing, up to the date of the issuance of the final order by the Commission.

Mr. Clay: May I ask what the Commission gets? They get the printed court record; do they?

[fol. 1208] Exam. Boyden: Yes.

Mr. Clay: Do they get the monthly earnings and the financial statement?

Mr. Gibson: They are printed in the court record.

Mr. Clay: Are they always printed?

Mr. Gibson: Always.

Mr. Clay: I see.

Mr. Anderson: Is that all that the Commission receives? Because I think the official court records are part of the

record in this case, and I am certainly not disposed to raise any technical question on the subject of it. If they were to send in papers, statistics, or anything of that kind, then, I think we might be in a different position. We would at least want to answer those statistics or cross examine them. Papers that go into the court records out there, we get those, but if they are sent into the Commission, court records, we don't, so it might put us in an awkward position. Is it court records that are printed and transmitted to this Commission?

Exam. Boyden: That is the way I get it, court records printed and transmitted to the Commission and filed in the docket.

Mr. Anderson: I have no objection to that going in the record, sir.

Exam. Boyden: I hear no objection.

[fol. 1209] WITNESS, T. A. THOMPSON

I hand you a statement which is entitled "The Denver & Rio Grande Western Railroad Company—Comparative Statement of Revenue Traffic Shown in Tons—Years 1920 to 1940, Both Inclusive," and I ask you whether that isn't merely an extention including the—whether that isn't the same as an exhibit which was introduced at the court hearing last August, except that it does show the 1940 figures?

A. That is correct.

Q. Otherwise, it is the same as RFC court Exhibit No. 1?

A. It is.

Q. This was prepared by you or under your direction?

A. It was.

Mr. Clay: Mark this Exhibit No. —.

Exam. Boyden: 272.

Mr. Clay: —272, and I offer it in evidence.

(Exhibit No. 272, Witness Thompson, marked for identification.)

By Mr. Clay:

Q. Will you comment on Exhibit 272 briefly? Does it now [fol. 1210] show that in 1940 there was a larger percentage

of the total revenue of traffic which was bridge traffic than in 1939?

A. It shows the larger tonnage of bridge traffic in the 21 years covered by the report.

Q. That is, in 1940 there was a larger percentage of bridge traffic than in any year in the last 20 years?

A. In the last 21 years; yes, sir.

Q. Well, that would seem to be merely an extension of the trend over this span of years?

A. It certainly indicates the trend.

Q. The trend, then, would seem to be over the long term an increasingly large percentage of bridge traffic and conversely a decreasing percentage of local traffic?

A. That is approximately correct.

Q. Now, at the court hearing last summer RFC offered an exhibit which is marked as Court Exhibit No. 10 which showed the freight revenue interchanged at Denver and at Pueblo, the two eastern gateways, for the years '37, '38 and '39.

I hand you now a statement entitled "The Denver & Rio Grande Western Railroad Company—Cars and Revenue of Freight Traffic Interchanged with Eastern Connections at Denver and Pueblo Gateways Received from and Delivered to the Southern Pacific at Ogden, Union Pacific at Provo, Salt Lake City and Ogden, and Western Pacific at [fol. 1211] Salt Lake City, Years 1937-1938-1939 and 1940.

I ask you if that was prepared by you or under your direction?

A. It was.

Q. The figures on the exhibit are correct, in accordance with the books of the trustees?

A. They are.

Mr. Clay: — this exhibit, which consists of two sheets, as Exhibit No. 273 and offer it in evidence.

(Exhibit No. 273, Witness Thompson, marked for identification.)

By Mr. Clay:

Q. Mr. Thompson, how can that differ in the main from the court Exhibit No. 10 which was offered at the court hearing last summer? It shows the 1940 figures; doesn't it?

A. There was added the 1940 figures and there was added the carloads in addition to the thousand dollars revenue for each of the connections named.

Q. That is, it shows the results net only in dollars, as did the previous exhibit, but also in carloads?

A. That is correct.

Q. Have you any comments on that exhibit?

A. No. I think it is self explanatory except to state that it assumes 1937 to be a hundred per cent and shows the ratio to 1937 for the following years, both by the Denver [fol. 1212] gateway and by the Pueblo gateway.

Q. That is, 1937 was a base year?

A. A hundred per cent, yes.

Q. A hundred per cent for each of the succeeding years.

Mr. Clay: That is all I have of this witness.

Exam. Boyden: Any cross examination?

Cross-examination.

By Mr. Anderson:

Q. Mr. Thompson, let us go back to that cash statement you have. You say that you had at the beginning of this year or the end of last year $4,328,000 in cash and you estimate that you will have at the end of this year, 1941, how much in cash?

A. $3,027,000.

Q. In other words, that you are losing a million, three hundred thousand dollars. Where did it go?

A. Well, most of it has gone into new equipment.

Q. You mean in paying—that is, equipment, on the capital expenditures on the property?

A. That is correct.

Q. And didn't you have in that amount last year some special deposits which you have since paid out in the matter of labor, taxes, or something of that sort?

A. A very, very small amount in last year's figures. No more than normal since '38.

Q. I see here you have got an item of special deposits of [fol. 1213] $480,169 on December 31st, 1940. Now, has that been paid out?

A. Very little of it.

Q. Have you still got that on hand, in addition to the three million that you estimated free cash?

A. I can give you the amount as of March 31st. To the extent that it includes the Railroad Retirement Act and Carriers Taxing Act, why, we accumulate that quarterly and pay it, see.

Q. Yes, I see.

A. There was approximately $185,000 in the special deposits on account of the retirement act and the Unemployment Acts as of March 31st, and about $155,000 in deposits of proceeds from the sale of mortgaged property, and that is substantially the same amount as we had at the end of the year.

Q. But you had $460,000 at the beginning of the year?

A. I have a comparison here of the breakdown. In the comparative special deposits of March 31st there was $1,450,000, because it included a deposit with the Pennsylvania Company for purchase of equipment.

Q. How much did you say for equipment?

A. It was $834,000 on deposit for purchase of equipment under an equipment trust.

Q. When was that deposited?

A. February 1st. That was the date of that equipment [fol. 1214] trust, series F.

Q. Now, have you made any deposits, or in your cash estimate have you made any provision for the cash payments on account of the $4,000,000 of equipment that Mr. Bradford testified has been ordered?

A. That is contemplated in the cash forecast, yes, all of it.

Q. And your reduction in cash from last year to this year of a little over a million dollars is attributable, you say, in large measure to payments on account of equipment?

A. That is right.

Q. You only pay 10 per cent on equipment?

A. 25 per cent on most of it in some of the cases. In some cases 10 per cent——

Q. How much are you paying this year for equipment? I mean not—on new equipment. I am not talking about old equipment trusts or anything of that kind.

A. Including what has already been paid?

Q. No. I am talking about the new cash payments which you make this year for equipment include that $800,000 in your percentage of——

A. That $800,000 includes the proceeds of the sale of the equipment trust certificates, series F.

Q. You have to pay that—when was that carried into your cash statement proceeds of the sale of equipment trust?

[fol. 1215] A. That was taken into cash in February.

Q. In February?

A. Yes, sir.

Q. And you have got to pay out that $800,000 during this year?

A. In fact, it has been paid out now.

Q. It is borrowed, a great deal of it?

A. 25 per cent of it was put up from the trustees' cash and 75 per cent proceeds.

Q. 25 and 75?

A. Right.

Q. So there is $200,000 there you have got to pay out. What other payments have you got to make on account of purchase of equipment during this year?

A. $1,425,000.

Q. In cash?

A. Right.

Q. That is $1,600,000 odd thousand dollars, then, you have got to pay out in new cash investments this year as against an increase in cash of about $1,300,000; isn't that true?

A. I don't know if I understand your question.

Q. In other words, you are paying out over $1,600,000 of new cash, of cash for new investment and equipment made during the year.

A. Right.

[fol. 1216] Q. As against a decrease of——

A. A million three——

Q. —in the cash, so your payments on account of equipment more than cover your decrease in cash?

A. That is correct.

Q. Now, does your cash contemplate that the accounts payable will be less or more at the end of the year than they were?

A. It contemplates being current on your accounts payable.

Q. Just current. As a matter of fact, last summer you than it really was; didn't you? You missed it by $800,000——

A. That is correct.

Q. —in July? That would be the first of the year. How does your estimate of the first three months of this year compare with the actual cash you had on hand from operations, and so on?

A. I don't know.

Q. In other words, did your income exceed your estimate by a hundred thousand dollars the first three months of this year?

A. Approximately a hundred thousand dollars, yes.

Q. And you have no way of saying that your income will exceed your balances for the rest of the year in the same proportion or in a larger proportion?

A. No. Nor can I say it might not show less.

[fol. 1217] Q. Now, had you not bought the new equipment, your cash at the end of this year would have been considerably more than it was at the end of 1940, wouldn't it, even on your own estimate?

A. No question about that.

Exam. Boyden: Mr. Thompson, you said, I believe, that your Exhibit 271 contemplates this $4,000,000 worth of new equipment that the company has now on order?

The Witness: That is correct.

Exam. Boyden: What items on it represent payments on that?

The Witness: Vouchers equipment, new locomotives, a total of $972,000; new passenger equipment $450,000. Now, the boxcars are behind us prior to May. They were contemplated in April.

Exam. Boyden: They have been paid for?

The Witness: Been paid for.

Exam. Boyden: Well, how much did the boxcars cost?

The Witness: $1,700,000, of which we paid $340,000 in cash—$440,000 in cash.

Q. How much is your equipment depreciation?

A. At the present time?

Q. Yes, for this year. How much do you carry in the way of equipment depreciation in a situation where you elect that in cash but do not——

[fol. 1218] A. Yes, I can figure it up. In round figures $1,200,000.

Q. I made it $1,250,000, but you make it $1,200,000. Now your equipment maturities are about $525,000 a year; aren't they?

A. You mean our present maturities?
Q. Yes.
A. About $670,000.
Q. $670,000?
A. Right.
Q. Well, that would leave you something over $500,000 out of equipment depreciation in cash; wouldn't it?
A. Right.

Mr. Clay: May I just clear up one more thing? You speak of your equipment maturity. That doesn't include the maturities of the $4,000,000 of the equipment trust?
The Witness: No; doesn't include the contemplated maturities.

By Mr. Anderson:

Q. I am speaking of this year. Now, that would give you, we will say, six hundred odd thousand dollars from that source. Now, you have an earning of $3,027,000 estimated; haven't you?
A. Income available for interest you mean?
Q. Yes.
A. Yes, sir.
Q. That is around $3,700,000 that you have got there [fol. 1219] from those two sources.
Now you take off your equipment trust certificate interest, $138,000, that would leave you the rest on that rough estimate $3,620,000; wouldn't it?
A. Right.
Q. So that on that basis you would have $3,620,000 of cash at the end of this year even if you only realized the income which you have estimated on those figures; wouldn't you, on those statements?
A. Go back over that again, please.

Exam. Boyden: Let the reporter read it.

(Record read by the reporter.)

By Mr. Anderson:

Q. What I am trying to get at is where you get rid of that million odd dollars is that thing there and how you make up your cash statement. $1,300,000 isn't very much these days, but it is a little pickings in a railroad like this.

A. Well, without the figures in front of me I can't say what the balance of the improvement program is, but there is a considerable amount in it. Of course, the improvement program is set up here just in ordinary vouchers.

Q. But at best your estimate of a little over $3,000,000 cash this year is after paying your new equipment percentage and based upon the assumption that your income will not exceed the forecast which you have made for the year,——

[fol. 1220] A. That is correct.

Q. ——although it did exceed it by $100,000 in the first three months?

A. That is correct.

Mr. Anderson: All right.

Redirect examination.

By Mr. Clay:

Q. Mr. Thompson, these three new Diesel engines which are going to cost a half a million dollars each are going to be delivered in January and February, 1942. Will you have to pay out any cash payment against those in 1941?

A. Not in '41; no.

Q. You have not allowed any cash payment?

A. Nothing for the new Diesels. Part on the new locomotives but not on the Diesels.

Q. What cash payment will be required against that million and a half expenditure, do you think?

A. That is not determined yet. It will either be a 10 per cent down payment up to possibly 25 per cent. We haven't been told, or I don't know as anybody has been asked to quote on them.

Q. Do you know if you can sell privately equipment trusts just on a Diesel engine? Isn't there a pretty high risk of destruction?

A. Based on our own experience and the commitment we have now——

Q. I mean a road haul engine; not a switch engine.

[fol. 1221] A. I think they will take the paper on a road haul engine as quickly as they will on a switch engine.

Q. What other railroad in the United States is using Diesel equipment on road haul?

A. Santa Fe is the only one I know of.

Q. Do you know if they financed it by an equipment trust or through cash?

A. I don't know.

Q. Of course, if you don't finance it through private channels you have got only two alternatives, selling the equipment trust to the R. F. C. or financing it with cash.

A. I don't think there is any question but what they can sell the paper.

Q. This estimate, of course, doesn't include any of the cost of the——

A. Of the Diesels.

Q. Of the three Diesels?

A. Of the three Diesels, no.

Q. And, of course, if you don't finance it through the R. F. C. or sell the paper for the cash, it would make it a million and a half in 1942, wouldn't it?

A. That is obvious if we had to pay for it in cash; certainly.

Q. You estimate that in 1941 you will have $3,027,000 on hand at the end of 1941. Assuming the reorganization is effectuated as of that time and the reorganization expense, counting not only the allowance, but the fees of in- [fol. 1222] corporating the company and recording the new mortgages and qualifying the company in different states, amount to $1,000,000, that $3,027,000 would be reduced to $2,000,000. Do you think that will be enough working capital for the reorganized company?

A. $2,000,000?

Q. Yes.

A. Ample.

Q. Would you want to get along to start the new company with less than $2,000,000?

A. I don't know that I am the proper man to say, but my own opinion is we could start with less than $2,000,000.

Q. Now, in the last few days there has been some mention in the newspapers that the five brotherhoods are asking for, I believe, a 30-per cent wage increase. You have made no allowance for that——

A. None whatever.

Q. —in this cash forecast or——

A. Income forecast either.

Q. Income forecast or any forecast that was made? Do you think $750,000 is a sufficiently large capital fund for

the combined system, that is, if you have a plan that consolidates the Denver & Rio Grande Western?

A. I don't think I am qualified to answer that question, Mr. Clay.

Q. Well, in a normal year will your additions and betterments run over or under $750,000?

[fol. 1223]

Mr. Anderson: I think you would have to define a normal year because there isn't anybody——

By Mr. Clay:

Q. Well, take the year 1942 when there will be no extraordinary improvements, when there will be no additions and betterments of an extraordinary nature.

A. I am just not qualified to answer that question.

Q. I think it was testified this morning that the improvement program, so far as roadway is concerned, is completed and the only thing left is making out some deferred depreciation on equipment. Would you think $750,000 would be enough for 1941?

Mr. Anderson: The witness has said twice he wasn't qualified to answer the question.

By Mr. Clay:

Q. Well, based on your experience.

Exam. Boyden: What official of the company is qualified to answer?

Mr. Anderson: What did you say, sir?

Exam. Boyden: I would like to know what official of the company is qualified.

Mr. Anderson: I don't think any of them are.

Mr. Clay: I submit, Mr.——

Mr. Anderson: I don't think any of them can guess better than I can or you can.

Exam. Boyden: Can any of them guess any better than Mr. Thompson can?

[fol. 1224]

Mr. Anderson: I think plenty of them can answer the question as to what the requirements are better than Mr. Thompson.

Exam. Boyden: Let us have Mr. Thompson give the best answer he can.

A. It is my own judgment that the property will always require a capital fund of $750,000 to $1,000,000.

Q. At least that much?

A. Based on the present accounting regulations.

Mr. Clay: That is all. We have another witness——

By Mr. Anderson:

Q. You spoke of the—you were asked about the question of financing your equipment. Is it not a fact that the manufacturers themselves finance these Diesel engines on monthly payments in addition to R. F. C. and the banking houses generally?

A. That is absolutely correct. In fact, we were offered affair rate of interest on the Diesels we are now buying and made better deals with the bankers.

Mr. Anderson: That is all.

By Mr. FitzGibbon:

Q. Mr. Thompson, did you, by any chance, in this forecast include any possible increase in rates?

A. None whatever. I presume you mean on revenue. No.

Mr. Clay: May I ask just one question?

By Mr. Clay:

Q. Did you allow anything for reduction of the $5,000,000 of outstanding trustees' certificates?

A. Nothing.

[fol. 1225] By Mr. Clay:

Q. Mr. Thompson, the question was raised as to how much Denver & Salt Lake stock was released by the RFC. I will ask you to turn to your Exhibit No. 276, and that exhibit shows a figure representing the amount of such stock as of November 1, 1935, and the amount of such stock held by the RFC as of March 31, 1941.

A. I have it. It shows released, 3,651 shares.

Q. Yes, that is right. That is the correct amount; isn't it?

A. That is the correct amount.

Q. We accept that as the correct amount. That answers the question of the Examiner. We have not information as to how many other shares may be actually outstanding with the public and we have no basis of obtaining that, unless the trustees will furnish it.

A. I can give it, if you will take my word for it. There are 430 shares outstanding and 30 shares in the treasury of the Denver & Salt Lake unissued under the plan of December, 1927. 460 shares in addition to the 3,100 shares under the Boettcher stock recision.

Mr. Clay: That is all.

Exam. Boyden: Exhibits No. 260 to 278, inclusive, are received into the record.

[fol. 1226] IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO, SITTING AT DENVER

No. 8669

In the Matter of the DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, Debtor

Excerpts from Final Hearing on Objections to Plan of Reorganization of Interstate Commerce Commission

(July 29 to August 12, 1940)

Be it Remembered that on, to wit, the 29th day of July, A. D. 1940, the same being one of the regular juridical days of the May, A. D. 1940, term of said court, this cause came on for trial before the Honorable J. Foster Symes, Judge of the District Court of the United States for the Judicial District of Colorado.

APPEARANCES:

Henry McAllister, Esq., for the Trustees of The Denver and Rio Grande Western Railroad Company.

Cass M. Herrington, Esq., and Curtis Heath, Esq., of the firm of Larkin, Rathbone & Perry, for the Central Hanover Bank and Trust Company, as Trustee.

Mason A. Lewis, Esq., of the firm of Lewis & Grant, and Arthur A. Gammell, Esq., and F. W. Wood, Esq., of the firm of Milbank, Tweed & Hope, for the Chase National Bank, as Trustee.

[fol. 1227] Ralph Hartzell, Esq., and John B. Marsh, Esq., of the firm of Mitchell, Taylor, Capron and Marsh, for City Bank Farmers Trust Company, as Trustee.

Messrs. Hodges, Vidal & Goree and Frank C. Nicodemus, Esq., for The Denver and Rio Grande Western Railroad Company, Debtor.

Erskine R. Myer, Esq., for the Trustee of the Denver and Salt Lake Western Railroad Company, Raymond L. Sauter, Esq., and the Moffat Tunnel Improvement District.

Robert G. Bosworth, Esq., of the firm of Pershing, Nye, Bosworth & Dick, and Thomas O'G. FitzGibbon, Esq., for the Guaranty Trust Company of New York, as Trustee.

Morrison Shafroth, Esq., of the firm of Grant, Shafroth & Toll, Henry W. Anderson, Esq., and George D. Gibson, Esq., of the firm of Hunton, Williams, Anderson, Gay & Moore, and Oscar R. Ewing, Esq., of the firm of Hughes, Richards, Hubbard and Ewing, for the Insurance Group Committee.

C. M. Clay, Esq., and Frederick E. Baukhages III, Esq., of Washington, D. C., and James A. Marsh, Esq., of Denver, Colorado, for the Reconstruction Finance Corporation.

Messrs. Gerald Hughes and Montgomery Dorsey, of the firm of Hughes & Dorsey, and W. A. W. Stewart, Esq., for the United States Trust Company of New York, as Trustee.

William L. Cohn, Esq., for the Untermyer Family Group.

James Quigg Newton, Jr., Esq., for the Ideal Corpora-
[fol. 1228] tion, C. Boettcher Investment Company, General Securities Company, and Charles Boettcher.

Thomas Keely, Esq., for the Western Pacific Railroad Corporation.

Byron G. Rogers, Esq., Attorney General, and James J. Patterson, Esq., Assistant Attorney General, for the Public Utilities Commission of Colorado.

Toll R. Ware, Esq., for Guy A. Thompson, Trustee of Missouri Pacific Railroad Company.

* * * * * * *

C. M. Lightburn, a witness called and sworn on behalf of the debtor, testified as follows:

Direct examination:

By Mr. Goree:

Mr. Anderson: In order that Court and counsel may be advised, I think it is my duty to state before the testimony begins that during the day I desire to ask leave of Court to file a motion, which I now make orally, to the effect that the Court dismiss this case, as provided it may do by the statute, because of the long delay in the prosecution of the case, and of the impracticability of obtaining a reorganization under Section 77 within a reasonable time, and [fol. 1229] permit the case, if the parties are so advised, to be brought in equity for the foreclosure of mortgages and the foreclosure of their contract rights. I am not proposing to argue that question at this time, nor shall I ask for a ruling of the Court on it until argument is made on the entire matter, but I think that the motion should be made at this stage to the end that the parties may be advised both in the presentation of their evidence and during the case.

The general grounds of the motion are that the bondholders of the property, not through any action of their own, because they did not come into court, but through the action of the debtor, have been deprived of any return upon their investment for a period of five years; that while it is recognized that under the decisions of the Supreme Court of the United States, the remedy of foreclosure may be suspended for a reasonable time, the security holders and creditors cannot be deprived of their contract rights indefinitely or denied their contract rights under the constitution. Therefore, as the plan before the Court for five years is wholly impracticable and will not be accepted by the security holders, and those whom I represent, it is our purpose to file a written motion to dismiss the proceeding and remove the injunction which now exists, and permit the creditors to proceed in accordance with their contract rights to enforce their respective liens in equity or proceed otherwise as they may be advised. I will file that motion later in the day.

The Court: It may be filed, Mr. Anderson.

[fol. 1230] Mr. Heath: Representing the Central Hanover Bank and Trust Company, as Trustee under the first mortgage of The Rio Grande Western Railroad Company and the first mortgage of The Rio Grande Junction Railway Company, we wish to join in that motion.

The Court: Decision will be reserved. You may proceed.

By Mr. Goree:

Q. Your name is C. M. Lightburn?

A. Yes, sir.

Q. You are Valuation Engineer for The Denver and Rio Grande Western Railroad?

A. I am.

Q. How long have you been connected with the Valuation Department of The Denver and Rio Grande Western Railroad?

A. Twenty-three years.

Q. In what capacities?

A. At first as Assistant Valuation Engineer. I have been Valuation Engineer since 1925.

Q. Have you prepared an estimate of the cost of reproduction of all properties of the debtor?

A. I have, with the exception of lands for transportation purposes, which is known as Interstate Commerce Commission Account No. 2.

Q. Tell us what consideration, if any, you gave to lands owned by the debtor.

A. I based my estimate of present value of lands on a joint reappraisal that we made with the representative of the Bureau of Valuation in 1937.

Q. Say whether you have prepared a statement showing the result of your study and work along this line.

A. I have.

(Thereupon a document was marked for identification as Objector's Exhibit 1.)

[fol. 1231] Q. I hand you paper which for identification has been marked Objector's Exhibit 1.

The Court: Do you offer this?

Mr. Goree: Not at this time, Your Honor. I will, after I have it explained.

Q. Now, tell us what that paper represents.

A. It first shows an estimate of cost of reproduction new

of units of property as of December, 1932, priced as of December, 1938. To this has been added the recorded cost of additions and betterments made during the period January 1, 1933, to December 31, 1938. Lands and rights, based upon the 1937 reappraisal, with net credit to Land Account for the period ending December 31, 1938, is then set forth. This credit is deducted from land values because of retirements in excess of land purchased prior to December 31, 1938. Next is included a computed value of equipment based upon the cost of reproduction less depreciation properly adjusted by additions and betterments to December 31, 1938.

Q. What was the starting point or basis for the beginning of your work, the results of which are shown by Debtor's Exhibit 1?

A. The work done in connection with the Interstate Commerce Commission under Section 19A of the Interstate Commerce Act commonly known as the Valuation Act.

Q. When was valuation work started on The Denver and Rio Grande Western Railroad under the Valuation Act?

A. In 1917.

Q. Tell us whether or not all this valuation was done on The Denver and Rio Grande Western after you came to it.

[fol. 1232] A. It was.

Q. Please tell us whether you are familiar with the manner in which all this work was done.

A. I am.

Q. Please tell us your connection, if any, with it.

A. I had direct charge of the valuation work from the very beginning. This included the time during which the inventory was made as well as all work subsequent thereto.

Q. Tell us how this work was done.

A. A joint inventory was made by representatives of the Bureau of Valuation and the carrier of all physical property, including road and equipment. Similarly a joint appraisal was made of all lands.

Q. Was the property of the debtor and its predecessor companies inventoried together, or were they divided up in any manner with the land?

A. The fixed physical properties, that is, lands, roadway, track, buildings, etc., was divided into valuation sections and subsections, and the inventory taken of the property in each section. Equipment was inventoried by classes for the entire system.

Q. Tell us what classifications, if any, were used in making this inventory of property of the debtor and its predecessor companies.

A. The property was inventoried according to the system of road and equipment accounts prescribed by the Interstate Commerce Commission.

Q. Taking first the road accounts, please tell us how the quantities were taken.

A. Cross-section parties were sent into the field to measure all gradings, bridges, trestles, culverts, rip-rap, ballast and other roadway quantities. Tie counts were made and [fol. 1233] weights of rail, kinds of frogs, switches, rails, etc. were recorded. Right-of-way fences, crossing signs, buildings, telegraph lines, signals, interlockers, and all other items of fixed physical property were measured or noted and recorded.

Q. Taking, now, the item of equipment, tell us, please, how the inventory of that item was made.

A. Representatives of the Bureau of Valuation and the carrier made a physical inspection and inventory of all equipment on the system, coordinating their observed data with the carrier's records. This was done by classes of equipment, that is, steam locomotives, freight train cars, passenger train cars, work equipment and miscellaneous equipment.

Q. Tell us just how the lands were handled in this inventory.

A. From maps previously submitted to the Bureau of Valuation by the carrier, the areas of all land parcels were determined and zones established. Lands of similar character and value were included in the same zone. A determination was then made of the unit values of similar adjacent lands, which was applied to the areas of the carrier's lands computed for each zone. The values for the zones were then assembled by valuation sections.

Q. Now, say whether or not values were then placed upon all these units of physical property.

A. They were.

Q. What was the valuation date of the debtor and its predecessor companies?

A. June 30, 1919, except for the Goshen Valley Railroad and The Denver and Salt Lake Western. These lines were built subsequent to the date of valuation.

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Vol. III

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Sup. Ct.

TRANSCRIPT OF RECORD

(Pages 897 to 1229)

Supreme Court of the United States

OCTOBER TERM, 1945

No. 278

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vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.

No. 279

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ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

PETITION FOR CERTIORARI FILED JULY 30, 1945.

CERTIORARI GRANTED OCTOBER 8, 1945.

SUPREME COURT OF THE UNITED STATES

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[fol. 1234] Q. In order to keep the record clear, please tell us the companies whose assets were inventoried as of the valuation date, that is, June 30, 1919.

A. The Denver and Rio Grande Railroad Company, which was the predecessor of the debtor, and The Rio Grande Junction Railway Company.

Q. Taking first the road accounts, tell us how the assets of The Denver and Rio Grande and of the Rio Grande Junction were valued, that is to say, were translated into dollars.

A. Prices were applied by representatives of the Bureau of Valuation to all units as recorded during the joint inventory. These prices were determined for the so-called normal pricing period of the years 1910 to 1914, inclusive. The effect of this was that quantities were taken as of June 30, 1919, and average prices for the period 1910 to 1914 were applied to these quantities.

Q. Referring still to the ad accounts, tell us whether you have given any consideration to any quantities which may have been added subsequent to June 30, 1919.

A. I have.

Q. Tell us the manner in which this was done.

A. All units of property added or retired from June 30, 1919, to December 31, 1932, were reported by us to the Bureau of Valuation together with their costs. Retirements of property were deducted from quantities recorded in the inventory and proper deductions made in the money total thereof. The costs of all units of property added, as reported by us to the Bureau of Valuation, were reduced by representatives of the Bureau to the 1910-14 price levels thus producing a sum of money for each account and for [fol. 1235] each valuation section which was added to the values already shown by valuation sections and accounts remaining in the original inventory.

Q. Tell us how the costs of quantities added subsequent to June 30, 1919, were reduced by the Bureau of Valuation to the 1910-14 prices.

A. For the units in most of the accounts and particularly those in the mass accounts, such as grading, bridges, ballast, etc., the 1910-14 prices as jointly determined and used in the inventory were applied to reduce the costs of units as reported for the period June 30, 1919, to December 31, 1932, to the 1910-14 base. For some of the accounts trend

factors or divisors were used. After careful study we accepted the Bureau's determination of these divisors as being approximately correct.

Q. State whether or not you checked the method used by the Bureau.

A. We did.

Q. What was the result of your check?

A. We accepted the Bureau's determination of these divisors as being approximately correct; that is to say, we accepted the Bureau's collection of units and repricing of these added units and their assembly with the units remaining in the inventory.

Q. Tell us whether you made any effort to determine the reproduction costs of these units of physical property as of December 31, 1938.

A. I did.

Q. Tell us how you did that.

A. Using the amounts of money as recorded by the Bureau for each account and for each valuation section as a base, [fol. 1236] we determined the index or multiplier for each element in each account by finding the relation of present day prices and costs to those of the 1910-1914 period. Then by determining the percentage relationship of the money in each account to the total roadway money for each valuation section we computed a composite multiplier which when applied to the 1910-14 money trended the money in each valuation section to the 1938 period.

Q. Describe to us the manner in which you have handled the additions and betterments made between December 31, 1932, and December 31, 1938.

A. I simply added our recorded costs for the units added during this period.

Q. Why did you handle these items in this manner?

A. Because after a study of prices for the several years in this period I was convinced that the average of the period would be reasonably close to the prices as of December 31, 1938. In other words, if the costs of these items had been trended to December 31, 1938, there would be no material difference in the result.

Q. Tell us, please, how you determined price levels as of December 31, 1938.

A. I studied all reports and data I could find relating to prices and costs current at that time, as well as prices and costs of prior and subsequent periods. For instance,

I found available reports of the Bureau of Labor Statistics and those of the Department of Commerce, including such data as "All Commodity" curve, "Cost of Living," cost data on metals and metal products, building materials and data for wages of unskilled and skilled labor. Also I had ac-
[fol. 1237] cess to current figures on recognized construction indices, including Aberthaw, American Appraisal Company, Tuttle, Associated General Contractors, and the construction cost index published by the Engineering News-Record. I also had before me our own current costs of construction materials and our Purchasing Agent's records as well as rates of pay for labor. Supplementing this information, I obtained opinions from reputable contractors relative to grading and other costs affecting our mass accounts, and obtained opinions from representatives of the equipment companies as to current costs and trends. As a means of relating cost data over a period of years, I used the railroad construction cost indices compiled by the Engineering Section of the Bureau of Valuation of the Interstate Commerce Commission, which are a result of joint studies continually made by representatives of the Bureau of Valuation and the railroads.

Q. You state that your study of prices included periods prior and subsequent to December 31, 1938. What was the length of time prior and subsequent to December 31, 1938, the prices of which you studied?

A. I studied indices and prices for a two-year period prior to December 31, 1938, and obtained all data I could find available subsequent to that date up to the present time.

Q. State whether this involved a great deal of labor on your part.

A. It required considerable time and study.

Q. State whether or not it is your duty as Valuation Engineer of the debtor to keep in touch with the trend of costs and prices.

A. It it.

Q. Were the prices as of December 31, 1938, which you [fol. 1238] determined the prices at which in your judgment the reconstruction work could be done for on that date, or do the prices represent an average for some period?

A. I determined as best I could period or average prices, rather than spot prices as of a particular date.

Q. State whether or not these prices for each road account were determined separately.

A. They were. In fact, the prices for each element in each road account were considered separately.

Q. Taking account 6, Bridges, Trestles, and Culverts, for example, tell us in detail how price-levels were determined.

A. The elements in account 6 of the Interstate Commerce Commission, Road and Equipment Accounts, Account 6, are: Dry Excavation; Wet Excavation; Masonry; Plain Concrete; Reinforced Concrete; Untreated and Treated Piling; Untreated and Treated Stringers; Untreated Bents; Hardware; Guard and Bridge Timber, Untreated; Bulk Head Timber, second-hand; I Beams; Deck Plate Girders; Trusses; Through Plate Girders; Cast Iron Pipe; Other Pipe; and Miscellaneous. Latest cost data studies for each of these elements were examined. Construction work in which the elements were involved was used as a guide in forming opinions as to current prices. The relationship of the money for the various elements to the total money in the account was used to ascertain the multiplier or trend factor for the account.

Q. State whether or not a similar process was used for the elements in each of the other road accounts.

A. It was.

Q. Was one price level for each of the elements in each [fol. 1239] account determined for all the debtor's property or for this purpose was the property of the debtor divided or segregated in any manner?

A. The property was divided by states and price levels ascertained for each element in each account in each state. That is to say, one price level for each element was determined for Colorado; another price level for each element was determined for Utah; and another price level for each element was determined for New Mexico.

Q. After this was done, what was the next step which you took in this work?

A. The property in each state had already been divided into valuation sections by the Bureau of Valuation of the Interstate Commerce Commission. After determining the index factor or multiplier for each roadway account, the relation of the money in each account to the total money for each valuation section was computed and a composite multiplier was thus determined for all the accounts in each valuation section.

Q. What method is used by the Bureau of Valuation of the Interstate Commerce Commission to keep its valuation of common carrier property up to date?

A. Order No. 3 of the Interstate Commerce Commission requires each carrier to report annually all the units of property and costs of additions and betterments and all retirements of property. The Bureau assembles these units with those of previous years and either reprices them at 1910-14 prices or trends the costs to that level by use of divisors. Thereafter for any particular date the Bureau finds price levels for the various elements in the various [fol. 1240], accounts and computes multipliers to be used in trending the assembled 1910-14 money to the date for which its valuation is being prepared.

Q. Then state whether or not the method used by you is similar to that used by the Bureau of Valuation.

A. It is.

Mr. Goree: May we ask that the record show that the exhibit heretofore referred to as Objectors' Exhibit 1 hereafter be referred to as Debtor's Exhibit No. 1.

Q. Referring now to Debtor's Exhibit 1, I notice under the heading Road Accounts, "Cost of Reproduction New, Owned and Used, Colorado—$86,575,726." Tell us just what that figure represents.

A. It is the cost of reproduction new of road accounts, excluding land, of all property of The Denver and Rio Grande Western in Colorado, as it existed on December 31, 932, trended to the December 31, 1938, price level in the manner I have described.

Q. And what does the figure of $46,933,577 just below it represent?

A. It represents a similar figure for the State of Utah.

Q. What does the figure $5,553,539 just below the Utah figure represent?

A. A similar figure for property in the State of New Mexico.

Q. Explain the next three items of that exhibit.

A. The figure $116,777 represents the debtor's portion of jointly used property in all states, determined in a manner similar to the foregoing. Likewise, the figure $38,510 represents the debtor's property jointly owned but wholly used by the debtor, determined in a similar manner. The [fol. 1241] next figure $244,825——

Q. Before we get to the next figure, you say that the figure $38,510 represents the debtor's property jointly owned. Is that the debtor's portion of that jointly owned property?

A. That is the debtor's portion in this case, and the one immediately preceding.

Q. Now, proceed.

A. The figure $224,825 represents the 1938 cost of reproduction new of all units for all states in Account 37, Roadway Machines.

Q. That is the Interstate Commerce Commission Account No. 37, the Roadway Machine account?

A. Correct.

Q. Explain the item of $139,462,954 which follows next on the exhibit.

A. It is the total of the items which I have just mentioned.

Q. Now, please explain the next entry, "Net Additions and Betterments, $927,028."

A. It is the net total of additions and betterments and retirements made to the debtor's property in the road accounts, except land, during the period January 1, 1933, to December 31, 1938. As I have explained above, these are actual cost figures and have not been trended for the reasons which I have already given.

Q. Tell us, please, what the next entry on the exhibit, $140,389,982, represents.

A. It represents an estimate made in the manner I have described of the cost of reproduction new of all the debtor's property embraced in road accounts, except land, as of December 31, 1938.

Q. Taking now the next heading on Debtor's Exhibit 1, "Lands," tell us what the first item, "Carrier, $4,662,445," [fol. 1242] includes.

A. It includes the value of all debtor's lands classified by the Bureau of Valuation as "Carrier" lands.

Q. That "Carrier lands" means land used for common carrier purposes, doesn't it?

A. As classified by the Bureau.

Q. By the Bureau of Valuation. What does the next item, "Non-Carrier, $1,207,704," include?

A. It includes the value of all the debtor's lands classified as "Non-Carrier" by the Bureau of Valuation.

Q. Please tell us how these values were determined and as of what date.

A. They were determined by a joint appraisal of all the company's lands made in 1937 by representatives of the Bureau of Valuation and a representative of the debtor.

Q. Why do you use the 1937 figures?

A. Because I did not believe it was necessary to make a reappraisal as of 1938.

Q. Explain your answer, please.

A. The change in unit values of lands between the latter part of 1937, when the reappraisal was made, and December, 1938, is so slight as to be negligible.

Q. Explain the next item on Debtor's Exhibit 1 entitled "Additions and Betterments to Land Account to December 31, 1938," showing a credit or deduction of $24,390.

A. This figure represents the net changes in costs of lands acquired and value of lands retired subsequent to the 1937 reappraisal and prior to December 31, 1938.

Q. Explain the next item, "Total Value of Lands to December 31, 1938, $5,848,142."

[fol. 1243] A. It is my best estimate of the value of the lands belonging to the debtor as of December 31, 1938.

Q. Just a moment, Mr. Lightburn, the figures there differ. Which is correct, the figure in the exhibit or the figure in your draft there? They differ slightly, you see.

A. The exhibit is correct.

Q. So that the total value of lands December 31, 1938, is $5,845,759, instead of the figure which you named previously?

A. Correct.

Q. Coming now to equipment covered by ICC accounts 51 to 58, inclusive, tell us how the cost of reproduction of the equipment belonging to the debtor was arrived at.

A. I determined the cost of reproduction new of equipment in a manner similar to that used in determining the cost of reproduction new of the road accounts—that is to say, I took figures compiled by the Bureau of Valuation showing the money in each equipment account they had previously reduced to the 1910-14 price level and trended this money by the use of indices or multipliers to December 31, 1938. This figure, then, represented the cost of reproduction new of equipment in existence as of December, 1935, priced to December 31, 1938.

Q. State whether or not you determined the cost of reproduction new of all equipment belonging to the debtor.

A. I ascertained the cost of reproduction new of all equipment belonging to the debtor company as of December 31, 1935, priced as of December 31, 1938, merely as a step in obtaining the cost of reproduction less depreciation.

Q. What did you determine to be the cost of reproduction [fol. 1244] new of the equipment belonging to the debtor on December 31, 1935, priced as of December 31, 1938?

A. 68,661,095.

Q. Dollars?

A. Dollars.

Q. Tell us how you developed the prices which you used in determining the cost of reproduction new of this equipment as of December 31, 1938.

A. All equipment on hand on valuation date, that is, June 30, 1919, was priced by the Bureau of Valuation on the basis of 1910-14 prices as heretofore explained. These prices were checked by me and with the exception hereinafter noted were accepted by us as proper for use in computing cost of reproduction new of our equipment as of June 30, 1919. All additions and betterments to these equipment accounts for the period June 30, 1919, to December 31, 1935, were repriced by the Bureau of Valuation or trended to the 1910-14 price base. From a study of 1938 prices as above explained, an index or multiplier was developed and by the use of this index or multiplier the money in the equipment account as of December 31, 1935, was trended to 1938 prices.

Q. Please tell us the method you used in determining the figure of $29,129,121, which is shown on Debtor's Exhibit 1 as the cost of reproduction less depreciation of this equipment as of December 31, 1938.

A. I ascertained the condition per cent of our equipment by taking into account the observed condition per cent stated by the Bureau of Valuation as of December 31, 1935. I also took into account extraordinary expenditures we had made for deferred maintenance of equipment during the years 1936, 1937, and 1938, and found a figure for cost of reproduction new of equipment in existence as of De- [fol. 1245] cember 31, 1935, priced as of December 31, 1938, of $29,873,489. To this figure I added the net changes in the equipment accounts resulting from retirement of old equipment and purchases of new equipment for the years

1936, 1937, and 1938. This amount I found to be $2,766,336, giving a total of $32,639,825. I then deducted accrued depreciation for the years 1936, 1937, and 1938, amounting to $3,310,704, and found the net cost of reproduction, less depreciation, of equipment as of December 31, 1938, to be the figure shown in this exhibit, that is, $29,129,121.

Q. In that answer you spoke of $29,873,489 as being the cost of reproduction new of equipment in existence on December 31, 1935, priced as of December 31, 1938. Is that correct, or is it cost of reproduction new less depreciation?

A. Cost of reproduction new less depreciation.

Mr. Goree: Debtor now offers in evidence Debtor's Exhibit No. 1.

The Court: Is there any objection? If not, it will be admitted.

Q. Have you prepared an estimate of the cost of reproduction new of all properties of The Rio Grande Junction Railway except Account 2, Lands for Transportation Purposes?

A. I have.

(Thereupon a paper was marked for identification Debtor's Exhibit 2.)

Q. I hand you paper, which for identification has been marked Debtor's Exhibit 2. Tell us what that paper represents.

A. It first shows an estimate of the cost of reproduction new of units of property as of December 31, 1932, priced [fol. 1246] as of December 31, 1938. This figure amounts to $4,751,301. To this has been added the net cost of additions and betterments made during the period January 1, 1933, to December 31, 1938, amounting to $479,881, making a total of $5,231,182 for the cost of reproduction new of the road accounts, except land, as of December 31, 1938. The value of lands for the period ending December 31, 1938, is then set forth in the amount of $69,384.

Q. Now, Mr. Lightburn, where is the Rio Grande Junction Railway located?

A. The termini are at Rifle and Grand Junction.

Q. Rifle and Grand Junction, Colorado?

A. Yes, sir.

Q. And they connect with what road at Rifle?

A. The Denver and Rio Grande Western at Rifle, and again with the Denver and Rio Grande Western at Grand Junction.

Q. Referring again to Debtor's Exhibit 2, state whether this paper shows the result of your work in determining the cost of reproduction new of all property of The Rio Grande Junction Railway Company as stated plus the value of its land as above set forth.

A. It does.

Q. Tell me the method used by you in arriving at the figures shown in this exhibit as the cost of reproduction new of the items of property in all of the road accounts except land.

A. I employed the same methods used in determining the cost of reproduction new of the road accounts, except land, as I did for The Denver and Rio Grande Western Railroad.

Q. Who was in charge of the valuation work of The Rio Grande Junction Railway?

[fol. 1247] A. I was. The inventory was made in connection with that of the debtor.

Q. What does the figure $5,300,566 as shown on Debtor's Exhibit 2 represent?

A. It represents the total cost of reproduction new of road accounts, excluding lands, as of December 31, 1938, plus the values of lands as of December 31, 1938, of the Rio Grande Junction Railway.

Mr. Goree: The debtor now offers in evidence Debtor's Exhibit 2.

The Court: Any objection? If not, it will be admitted.

Mr. Goree: For the purpose of the record, I will say that the value of the Rio Grande Junction Railway Company shown on Debtor's Exhibit 2 is not included in the cost of reproduction of the Denver and Rio Grande Western Railroad, as shown on Debtor's Exhibit 1. I will later introduce an exhibit which summarizes these different costs and values.

Q. Mr. Lightburn, where is the Goshen Valley Railway located?

A. It is a branch line over in Utah extending into one of the mining districts, close to the Tintic Mining District.

Q. What are its termini?

A. It runs from Pearl Junction, a point on the main line of the Rio Grande, to Dividend.

Q. That is on the main line of the debtor, Pearl Junction, is that right?

A. Yes, sir, it is.

Q. Have you determined the cost of reproduction new of the items of property in the road accounts of the Goshen Valley Railway Company, except lands?

A. I have.

(Thereupon a paper was marked for identification Debtor's Exhibit 3.)

Q. I hand you a paper which has been identified as Debtor's Exhibit 3. Is the result of that work shown on that exhibit?

[fol. 1248]

A. It is.

Q. Tell us the manner in which that work was done.

A. The Goshen Valley Railroad Company was not built at the time of the ICC inventory. Therefore, all quantities and costs were reported to the Bureau of Valuation following construction, in accordance with Valuation Order No. 3 of the ICC. Thereafter the Bureau reduced our reported costs to a 1928-1927 price base, rather than the 1910-14 price base. We reviewed this method of procedure and ascertained that it produced a result that was approximately correct for the pricing period 1923-1927; at least, it was certainly not too high. In developing multipliers for the road accounts, except land, for Goshen Valley we determined the relation between the price level in 1923-1927 and that of December 31, 1938, and applied these multipliers to the units of property of the Goshen Valley. Application of multipliers produced a cost of reproduction new as of December 31, 1932, of $360,777. Net additions and betterments for the period January 1, 1933, to 1938 are recorded in the amount of $208, which makes the total cost of reproduction new as of December 31, 1938, $360,985.

Q. Please tell us how the figure $3129 shown as the value of the lands of the Goshen Valley Railroad was arrived at.

A. This figure is a result of a joint reappraisal of the lands of the Goshen Valley as of 1937 by representatives of the Bureau of Valuation and the debtor.

The Court: How long is that railroad?

The Witness: It is six or seven miles.

[fol. 1249] Q. Then what does the figure $364,114 shown on Debtor's Exhibit No. 3 represent?

A. The cost of reproduction new of the road accounts, except fuel, of the Goshen Valley as of December 31, 1938, plus the appraised value of the lands of that carrier.

Q. You state that the lands were appraised in 1937. What would you say as to any change in their value between the date of their appraisal in 1937 and December 31, 1938?

A. The change in value, if any, would be negligible.

Mr. Goree: If Your Honor please, the debtor now offers in evidence Debtor's Exhibit 3.

The Court: It will be admitted, if there is no objection.

Q. Mr. Lightburn, we come now to the Denver and Salt Lake Western Railroad Company. Tell us, please, where that railroad is and its termini.

A. The termini are Bond, or a point near Bond known as Orested, on the Denver and Salt Lake, and Dotsero, about eighteen miles this side of Glenwood Springs on the Denver and Rio Grande Western.

Q. Both of these points are in the State of Colorado, of course?

A. Yes, sir.

Q. How long is that line?

A. Just a little over 37 miles.

Q. When was it built?

A. In 1934.

Q. State whether you have prepared an estimate of the cost of reproduction new of all properties of the Denver and Salt Lake Western Railroad Company.

A. I have, with the exception of Lands for Transportation Purposes which is known as ICC Account No. 2.

[fol. 1250] Q. Tell us what consideration, if any, you gave to lands owned by the Denver and Salt Lake Western Railroad.

A. I based my estimate of present value of lands on the joint reappraisal that we made with the representatives of the Bureau of Valuation in 1937.

Q. Have you prepared a statement showing the result of your study and work along this line?.

A. I have.

(Thereupon a paper was marked for identification Debtor's Exhibit 4.)

Q. I hand you a paper which for identification has been marked Debtor's Exhibit No. 4. Please tell us what that paper represents.

A. The first figure appearing on this exhibit—that is, $4,597,003—is the estimated cost of reproduction new of road accounts of the Denver and Salt Lake Western, except land.

Q. How was this figure obtained?

A. Recorded costs of the property as reported by the carrier to the Interstate Commerce Commission for all road accounts, except land, were trended from the date of construction in June 1934, to December 31, 1938.

Q. When the original cost figures were trended to December 31, 1938, as stated by you, what result was obtained?

A. A cost of reproduction new of $4,597,003 was found for units of property as constructed and turned over for operation June 16, 1934, priced as of December 31, 1938.

Q. What does the item "Additions and Betterments, $106,188" represent?

A. It represents recorded costs of additions and betterments made to the property between June 16, 1934, and December 31, 1938.

[fol. 1251] Q. From your familiarity with prices and your studies of the trends of prices, as heretofore explained, would you say that the cost of these additions and betterments would be increased or decreased if this cost figure of $106,188 had been trended to December 31, 1938?

A. The difference between the recorded cost of these improvements and their cost of reproduction as of December 31, 1938, would be negligible.

Q. Explain the item, "Land, $12,719."

A. This figure resulted from the joint reappraisement made by a representative of the Bureau of Valuation and the debtor in 1937.

Q. What would you say as to the difference, if any, in the value of these lands in 1937 and on December 31, 1938?

A. There would be little, if any, difference in their value between 1937 and December 31, 1938.

Q. And December, 1938?

A. December, 1938.

Q. State whether or not you considered the figure of $12,719 a fair appraisal of the valuation of the lands of the Denver and Salt Lake Western Railroad as of December 31, 1938.

A. It is a fair appraisal based on the Bureau's methods of land appraisal, that is, comparing the lands to similar adjacent lands. I will say, however, that the figures are much less than the cost of the lands to us at the date of acquisition, less than five years previous.

By the Court:

Q. In other words, it is your testimony that that strip of land from Dotsero to Bond is only worth $12,719?

A. That, your Honor, is the way it has been appraised by [fol. 1252] the Bureau of Valuation. Its actual cost was something over $93,000.

Q. This is not your valuation. You are testifying to that of the ICC?

A. I am testifying that is a fair figure of appraisal based on their methods of comparing a right-of-way with similar adjacent lands, because, as we all know, similar adjacent lands up there are not worth very much in that rough country. It does not represent anything at all of a relationship to its cost.

Q. Was there any condemnation?

A. We had very little condemnation. We purchased it just as any railroad purchases land. When people know that they need the land, they pay what people think they can get for it.

(Thereupon a recess was taken until 2 o'clock p. m.)

[fol. 1253] Pursuant to recess the following proceedings were had at two o'clock p. m.:

C. M. LIGHTBURN resumed the stand for further

Direct examination.

By Mr. Goree:

Q. Mr. Lightburn, this morning you testified about the length and termini of the Goshen Valley Railroad Com-

pany. Have you refreshed your mind on that, and wish to make any correction?

A. Well, my answer I think is correct, but someone thought that it had not been understood by the reporter. I said the length of the Goshen Valley was between six and seven miles. It is actually—the main spur is 6.52 miles. There is another spur called the King spur that is 2.27 miles long.

Q. Do they lead from the main line of The Denver and Rio Grande or from some branch?

A. They lead from the main line of the Tintic branch.

Mr. Goree: If your Honor please, just before adjournment I had offered in evidence Debtor's Exhibit 4 to which there was no objection, but the reporter tells me that your Honor did not rule on it, and I would just like to have the record show it was admitted.

The Court: It will be admitted if there is no objection.

Mr. Goree: That is the Denver and Salt Lake Western.

Q. Now, Mr. Lightburn, on Debtor's Exhibits 1, 3 and 4 I notice that no equipment is shown. Explain this omission, please.

[fol. 1254] A. The Rio Grande Junction, the Goshen Valley and the Denver and Salt Lake Western own no equipment.

Q. In your opinion do the figures heretofore submitted by you as the cost of reproduction of all properties, except land, of these carriers, plus the values of their lands, and, in the case of the Denver and Rio Grande Western, plus the value of its equipment, completely represent the value of their assets?

A. No.

Q. Explain your answer.

A. In my opinion the increments and elements of value residing in these properties should be added in the determining of their total value as operating properties.

Q. What are the increments or elements of value to which you refer?

A. The debtor, for example, has the right to use telegraph lines along its right-of-way and enjoys an easement right in these lines that is nowhere included in cost of reproduction. In my opinion the value of this right should be no less than the estimated cost of reproduction of improvements turned over to the Western Union Telegraph

Company under an agreement dated August 22, 1917. The estimated cost of reproduction of these improvements is at least $300,000. The debtor possesses valuable water rights and lands acquired in irrigated territory that have been under-appraised by the Bureau of Valuation. My estimate for this increment is $465,559. The full value of these water rights was not included in the cost of reproduction figures heretofore given because there was a disagreement between the debtor and the Bureau of Valuation [fol. 1255] as to principle in the manner in which they should be inventoried. Similarly, the debtor's lines occupy many miles of mountain passes, gorges and canyons. These rights-of-way are especially favorable and advantageous for railroad uses on account of their peculiar topography and strategic location. No adequate value of these canyon rights-of-way have been allowed by the Interstate Commerce Commission. In my opinion, not less than $3,108,000 should be added as the value of these canyon rights in excess of the amounts shown as the value of lands in the exhibit heretofore presented. The additional values of these canyon rights are not included in those exhibits because of a disagrement between the debtor and the Bureau of Valuation. There was also a disagreement between the debtor and the Bureau of Valuation——

Q. Well, what was that disagreement between the debtor and the Bureau of Valuation that you spoke of? Was that as to the principle as to the manner in which they should be appraised?

A. Surely. It was represented in the testimony I gave this morning regarding the Dotsero Cut-off. They appraised the lands adjacent to these canyons at a nominal figure. We claim that those canyons are worth more than that.

Q. Continue, please.

A. The figures which I have included in Debtor's Exhibit No. 1 on account of equipment for the debtor follows the principle approved by the Bureau of Valuation, but in my opinion an additional value of not less than $237,000 should [fol. 1256] be added to the cost of reproduction less depreciation of equipment.

Q. Was that because of a disagreement between the Debtor and the Bureau of Valuation as to the manner in which certain narrow gauge equipment should be appraised?

A. It was.

Q. Proceed, please.

A. All these increments of value should properly be allocated to reproduction costs or to values of lands of the debtor.

(Thereupon a document was marked Debtor's Exhibit 5 for identification.)

Q. In your opinion, do the costs of reproduction as shown by your various exhibits, plus the increments of value just mentioned, adequately cover the value of the properties of these carriers?

A. No.

Q. Why not?

A. There are other elements of value inherent in these railroad properties which should be added in order to determine their final value.

Q. What are these other elements of value that you mention? Explain them in detail.

A. The cost of development of the property, going concern value and development of business. If the properties of the carriers were reproduced new they could not be developed in the way that the properties of the carriers now are, and to develop them to the present point of efficiency would entail considerable expense. In addition to the cost of reproduction of the physical property of the Rio Grande as it exists at the present time, it would be necessary to incur certain expenditures in the development thereof, [fol. 1257] such as the excess cost over and above ordinary or normal maintenance costs during the early years of operation, the excess cost of opening out ditches and keeping them open during the early period of operation, and replacing and maintaining the slopes of cuts and fills, the cost of relocating and adjusting waterways and other roadway openings in conformity with experience gained as to the proper location and size of these openings which became manifest after the beginning of operation; the cost of developing gravel pits; the cost of testing for and developing suitable and adequate water supply based on the experience requirements of early operation; excess costs made necessary during the first years of operation by the occurrence of floods, rock slides, wash-ins and snow slides, and the extraordinary cost of protecting and policing tracks and roadbed through the mountains during the time the

roadbed is unstable and more vulnerable to the hazard of natural causes; the cost, after the beginning of operation, of raising grades and effecting line and channel changes; the excess cost of building snow fences and other protective devices in excess of what similar construction would cost under normal conditions; the excess cost of designing, determining and evolving the proper motive power and other equipment to meet operating conditions peculiar to the territory; the cost of determining the proper location, character and capacity of engine and division terminals, helper stations, and the cost of determining proper locations for passing tracks and other side tracks. Another item is the excessive cost of operating the newly constructed roadbed. The full service of locomotives cannot be obtained, [fol. 1258] and costs of train movements are manifestly excessive on a new track. All these are truly development costs, and we maintain that on this account a sum of no less than $9,000,000 should be considered as an element of value as of December 31, 1938. As to "Going Concern Value," assuming that the physical property of the Denver and Rio Grande has been constructed new and ready for operation as of any particular date, which is the assumption under the reproduction theory of the Bureau of Valuation, it is also necessary to assume that the personnel would be assembled and trained prior to that date, ready for the operation of the new system. It takes time and much effort to assemble, train and co-ordinate such a group. It would be necessary to first analyze the character, volume, origin and destination of the traffic actually to be offered for transportation as well as the potentially available traffic. Second, it would be necessary to determine the character and number of officers and employees necessary to handle the business and maintain the property. During this organization period it would be necessary to design, publish and distribute time tables, tariffs, fares, correspondence, accounting and other classes of forms, leases and agreements, maintenance standards, prepare and install rules, instructions and practices for all concerned, and to codify and arrange for compliance with all regulatory acts of political divisions. The cost that would have to be met to get reproduced property into effectual operation as a common carrier would be not less than $7,000,000. We think that on that account an additional element of value of not less [fol. 1259] than that amount exists. As to development of

business; the development of the freight and passenger traffic of the debtor as it existed on December 31, 1938, would represent a substantial outlay; which in my opinion would not be less than $550,000. This is an additional element of value which should be considered in arriving at a valuation of the properties of the debtor, and I am of the opinion that on that account the sum of $550,000 should be added.

(Thereupon a paper was marked for identification as Debtor's Exhibit No. 6.)

Q. Has the Debtor any other assets which should be considered in placing a value upon these properties?

A. Yes, it has various stockholding interests in or has made advances to certain companies that are necessary to its operation. Among these are terminal companies, motorway bus and truck lines, The Railway Express Agency, The Denver Market and Produce Terminal, Inc., and The Utah Fuel Company. The detail of this is shown on Debtor's Exhibit No. 6.

Q. Without taking into consideration the values of the stockholding interests in and advances to the companies just mentioned, what would you say is the fair combined value of the properties of the debtor, of the Rio Grande Junction Railway, of the Goshen Valley Railroad Company, and of the Denver and Salt Lake Western Railroad?

A. $206,406,318.

Q. This value is as of what date?

A. December 31, 1938.

Q. Why was this date chosen by you?

A. Because of its proximity to the date of the plan, and because it was the latest date for which adequate and re-
[fol. 1260] liable cost data were available.

Mr. Goree: The debtor now moves that Debtor's Exhibit No. 5 be admitted in evidence, Your Honor.

The Court: It may be admitted.

(Debtor's Exhibit No. 5 is attached hereto and made a part hereof.)

Q. In arriving at this figure, have you added anything on account of the interests in or advances to the various companies listed in Debtor's Exhibit No. 6?

A. I have not.

Q. Are you able to do this now?

A. No, I am not.

Q. Why not?

A. The time for preparing this was so short and any appraisal of these interests would entail so much work that I deemed it best not to attempt it. In any event, these stockholding interests and credits would increase the value which I have named for the properties of the Debtor.

Q. When and if their values are ascertained, what would you say should be done with those values?

A. They should be added to the values of the property of the Debtor which I have stated.

Mr. Goree: At this time, if Your Honor please, the Debtor moves that Debtor's Exhibit No. 6 be admitted in evidence.

The Court: Without objection, it may be admitted.

Q. In placing a value upon the properties of the Debtor have you given any consideration to cash on hand, materials and supplies, and so forth?

A. Yes, I have considered them, but current assets and current liabilities approximately offset one another so I [fol. 1261] did not think there was any net value to be added on this account.

Mr. Hodges: May it please the Court, at this point in Mr. Lightburn's testimony, while Debtor's Exhibit No. 6 is being introduced, I call attention to the Utah Fuel Company stock listed at a book value of one dollar, and I call the attention of the Court to the fact that the record certified here by the Interstate Commerce Commission carries the testimony of expert engineers as to the value of the Utah Fuel Company's stock, placing a value of $4,600,000, approximately, on the Utah Fuel Company's Stock.

(Thereupon a paper was marked for identification Debtor's Exhibit No. 7.)

Q. Have you attempted to allocate the cost of reproduction of physical property of The Denver and Rio Grande Western Railroad Company, to the various mortgage divisions of that Debtor? When I say the estimated cost of reproduction of the physical property, I mean the estimated cost of reproduction of the road accounts, plus the estimated costs of reproduction, less depreciation of equipment, plus the value of lands as of December 31, 1938.

A. I have.

Q. I hand you Debtor's Exhibit No. 7. What is that paper?

A. The first column is an allocation of the costs of reproduction, new, of the units of property in the road accounts as of December 31, 1932, priced as of December 31, 1938. The total is the same figure appearing in Debtor's Exhibit No. 1. The second column shows additions and betterments applicable to the road accounts. The third column is the total of the road accounts as of December 31, [fol. 1262] 1938. The value of the land is set forth in similar manner, the first column being 1937 appraisal about which I have heretofore testified. The following column shows additions and retirements to December 31, 1938, and the following column shows the total land values as of December 31, 1938. The equipment column shows an approximate allocation of units of equipment to the several mortgages as of December 31, 1938. The total shows the property in all accounts as of December 31, 1938.

Q. Tell us how the costs in the road accounts were divided among the several mortgage divisions:

A. This was done by taking the valuation sections or parts of valuation sections of the road covered by each of the several mortgages.

Q. Say whether the costs in the road accounts assigned to the several mortgages are those inherent in the property on which the respective mortgages are first liens.

A. They are.

Q. The fact that the Debtor's line of railroad was divided for valuation purposes into valuation sections made this allocation comparatively easy, did it not?

A. It did.

Q. Tell us now how the land values were divided.

A. The land values were divided in the same manner as the road accounts were allocated; that is, the valuation sections or parts of valuation sections upon which the sevral mortgages were first liens respectively.

Q. What do the equipment costs used in this exhibit represents?

A. The cost of reproduction, less depreciation, of the equipment as of December 31, 1938.

Q. How were these costs divided among the several mortgage divisions?

A. It was impossible to obtain accurate allocation figures subsequent to 1935, so percentages were obtained on the [fol. 1263] 1935 allocation figures and those percentages were applied to the total valuation of equipment figure previously testified to for December 31, 1938, which appears as a total figure for the equipment in this column. Subsequent adjustments resulting from agreements between the bondholders of the various issues were reflected as accurately as possible. While these allocation figures are at best an approximation, they are the best approximation *that we could* make, and the total equipment figure is correct as previously testified to.

Mr. Goree: If the Court please, we offer in evidence Debtor's Exhibit No. 7.

Mr. Anderson: If Your Honor please, we object to the introduction of that exhibit on the ground that it constitutes no basis of ascertainment of commercial value or reorganization value. We have let the general figures go in without objection on the views of the Debtor, but when it comes to undertaking the distributions between bondholders' and mortgage divisions, both roadway and equipment, we do not think they are applicable, and we do not think they are of any value whatever for that purpose. We, therefore, object to it, and we do not think the distribution is sound; in other words, the witness himself has said it is only an aproximation, and an approximation is not sound.

Mr. Fitzgibbon: If the Court please, I should like to enter our objection, and also state this, with regard to the matter of equipment: There is some sort of an understanding among the bondholders, which has been referred to here. The Trustee that I represent has never been a party [fol. 1264] to that, and as a matter of fact, contests that allocation; therefore, we say there is really no basis as made in the allocation of that equipment.

Mr. Anderson: I move to strike out the allocation of equipment, if the exhibit is admitted, and I object to it entirely.

Mr. Heath: If the Court please, our company as Trustee of the first mortgage, would like to offer the same objection.

Mr. Hodges: The introduction of this exhibit is not of great moment to the Debtor. It is introduced because it may be useful to the parties in this cause before they get through, as it is a correct allocation, and stated to be, of

road construction. Unfortunately, the impossible cannot be done. Equipment cannot be allocated at this moment, nor until the record is finally settled, as to who is entitled to the typical items of equipment. There was an agreement between some of the bondholding representatives, which seems to have been relied upon by the Interstate Commerce Commission. This exhibit adheres to that as nearly as possible, although there are some additions to equipment since the date of that agreement and the allocation by the ICC which make it somewhat uncertain. Now, it is true that the bond issues represented by the Guaranty Trust Company and possibly the Hanover—I don't know whether there was any contest between the Hanover and any of the other Trustees as to equipment—but I think it is true that those bond issues represented by the Guaranty did not agree to the allocation, but there is still the legal question [fol. 1265] for this Court to decide as to what the proper allocation shall be. Of course, the Court is not bound by this exhibit. This exhibit is tendered in good faith as something that we think is useful, and perhaps the Court will find it useful, and it is a useful collection of statistics on the basis of this witness' testimony as to the total valuation.

The Court: It will be admitted, the probative value of it to be determined later. Proceed.

Mr. Goree: That is all the examination in chief.

The Court: Mr. Hodges, you claim the allocation of equipment was never agreed to?

Mr. Hodges: I suppose it would not be sound to claim it has been agreed to. There was an understanding as between certain parties interested which seemed to carry that far, but that cannot bind other parties who did not agree.

The Court: What evidence is there of that agreement?

Mr. Hodges: That is in the briefs before the Interstate Commerce Commission, and I think there is a reference to it in the Interstate Commerce Commission's report.

I want to ask the witness one question:

By Mr. Hodges:

Q. Have you examined these reproduction value figures to determine the result if you carried forward two years from 1938, or if you carried your period back two years from the time when you began it, what effect it would have on the valuation?

A. Construction costs are ascending right at the present time. They have ascended almost steadily since 1937; and I believe that the December 31, 1938, value is a fair average of the period of approximately four years. To go back [fol. 1266] before that time, why, that is a different story.

Mr. Anderson: May I ask the witness a question?

The Court: Surely.

Cross-examination.

By Mr. Anderson:

Q. As I understand, your valuation here has followed generally the process followed by the Interstate Commerce Commission in arriving at value for rate making purposes; is that correct?

A. That is correct, yes, sir.

Q. You do not contend at all that the value as stated by you upon the formula arrived at by the use of the formula of the ICC is any representation of the commercial value of this property or of its value for reorganization purposes, do you?

Mr. Hodges: I object to the question as calling——

Mr. Anderson: I have the right to go to the bottom of the well.

Mr. Hodges: You have a right to go to the bottom of the right well, but not the wrong well. This witness has testified to the reproduction costs of this property and its accrued depreciation. The question which your Honor has to consider and determine is the solvency of this Debtor. This witness does not pretend to tell your Honor what the answer is to that question, nor is his opinion of any concern to your Honor. He has testified to these basic facts that are essential for the establishment of reproduction costs, and accrued depreciation is a material thing. It is for your Honor to determine whether that represents the material value to be considered, and the issues in this case could not be controlled by the witness' opinion as to whether that [fol. 1267] value was of any importance.

The Court: What is the question?

Mr. Anderson: I might state, to save time, I asked him if he contended that this valuation which he had made on the formula of the ICC was related in any way to the value

of the property for commercial purposes or for reorganization purposes. I want to see if he meant that the two applied, because he uses the term "value" very often without designating what he means.

The Court: The objection is overruled.

Mr. Hodges: I save an exception.

A. The value, Colonel Anderson, was determined generally upon the method of procedure used by the Interstate Commerce Commission, Bureau of Valuation. That method has been used and might be used to determine the commercial value of the property. I have known it to be used.

Q. When and where?

A. In the purchase of property that the Debtor company has purchased heretofore we used approximately that value to determine how much we would pay for the property.

Q. How much you would pay for what kind of property?

A. Railroad property.

Q. Well, I mean land——

A. Land, rails, roadbed.

Q. You mean, for the purchase of a road, that you took the ICC value as representing the commercial value?

A. We used the same methods to determine it; we used the same methods in determining values for contract purposes upon which we earned. On that basis I would say it would be useful as a means of determining commercial value.

Q. Then do I understand you to say that when you use [fol. 1268] the term "ICC value" here, that you mean commercial value or mean value for reorganization purposes of this property?

A. I perhaps misunderstood you, but I thought we were discussing the method of approach.

Q. No; I asked you if you meant your term "value," frequently used throughout without any limitation, to apply to reorganization value or commercial value of property.

A. My answer is intended to mean that it could be and has been and is being used as a means of determining——

Q. That does not answer my question. I asked you what you meant by it. I am talking about your evidence, not what somebody else said. Is your testimony confined entirely to reproduction new where you use the cost less depreciation?

A. Plus these other items of value, yes, sir.

Q. That is all you were talking about?

A. Yes, sir.

Q. And you are not undertaking to define or to state commercial or reorganization values, are you?

Mr. Hodges: I think that is a most unfair procedure that you are asking this witness to indulge in.

Mr. Anderson: It is proper cross-examination.

Mr. Hodges: It is not proper cross-examination at all.

Mr. Anderson: I am trying to get what he is talking about.

Mr. Hodges: He has told you what he is talking about. You are asking for his opinion as to the relevancy of reproduction cost in determining the question which the Court has to determine.

Mr. Anderson: I submit I did not ask his opinion upon [fol. 1269] the testimony as to relevancy. I asked him what he meant by his term "value," which he has used over and over again, without any reference to any limitation, and I say you were confining your statement to the reproduction value as defined by the Interstate Commerce Commission for rate making purposes and you do not undertake to testify as to the commercial value or value for reorganization purposes, and I want an answer to that question. That is a perfectly legitimate question in order to interpret his evidence before the Court.

The Court: What is reorganization value? It has not been defined.

Mr. Hodges: I never saw it defined.

Mr. Anderson: I will argue that question at the proper time. The reorganization of a railroad is substantially the same as a railroad now. It is not reproduction cost less depreciation for rate making purposes, and has been so stated a number of times.

Mr. Hodges: It was stated to the contrary by Judge Coleman in the case I introduced.

Mr. Anderson: I am entitled to have the witness say what he is talking about at least.

Mr. Hodges: You are not entitled to a conclusion from this witness, and you are asking for a conclusion.

The Court: He may answer the question if he can.

A. I have endeavored to answer it. It is true that we use the methods on which the Interstate Commerce Commission

approached the matter of value when they started out to determine the value for rate making purposes, but we did [fol. 1270] not follow their methods entirely because they would probably use cost of reproduction less depreciation all the way through. We tried to find a value for the property. I don't know whether it is commercial value or reorganization value. And I will say that we have used these same methods for commercial purposes.

Q. Well, now, you have started to answer what my next question will be. You stated that you followed the ICC method of valuation for rate making purposes, in reply to my first question.

A. Not entirely, because——

Q. Now, you say you followed it in part, and did not follow it in part. That being true, I would like to know what you followed in part that you didn't follow on the formula. What did you follow there?

A. Their method of valuation for rate making purposes started out with cost of reproduction less depreciation. They allowed working capital. I didn't take cost of reproduction less depreciation. I took cost of reproduction new on the road accounts, and didn't take into account any working capital. They are the essential differences.

Q. You didn't depreciate the road at all?

A. Not at all.

Q. You just took it as if it was built today, new, absolutely new, new rails, new cross ties, new equipment, new everything. Is that right?

A. Correct.

Q. Now, what formula did you apply, if you didn't apply the ICC formula, in arriving at your value all the way through? I mean, you applied the ICC formula up to a certain point and then stopped. Now, what formula did you apply after that?

[fol. 1271] A. Well, it wasn't really a formula. We just followed their method, except we didn't use cost of reproduction less depreciation of road, for the reason that it is our theory that if a road is properly maintained, there is no depreciation in the road account.

Q. And you don't think that this road did depreciate at all from a new railroad, that a railroad built December 31, 1938, or December 31, 1932, we will say, is just as good as a new railroad; is that your idea?

A. No, that is not exactly my idea.

Q. What is your idea, if that is what you valued? You gave your value as of those dates.

A. In some places it might be better. It might be you had renewed structures and bridges. Some places might be very much worse.

Q. Can a bridge be better than a new bridge?

A. Yes, it might be better than one originally put in there and a track—

Q. I am not asking you that. You are talking about reproduction new today. Could a bridge be better than a new bridge today?

A. No.

Q. Could a track be better than a well-constructed new track today?

A. Very much so.

Q. It could be settled, you mean?

A. Yes, sir.

Q. You couldn't make it any better for construction purposes?

A. It would be better after a number of years than when you first built it.

Q. Well, the rails would be new, all the ties would be new. They would be better when they were new than after they were used. The elements of the track would be better, the only difference would be they hadn't settled as com-
[fol. 1272] pletely as an older track, but by the time they had settled they would have worn some, wouldn't they?

A. You mean the roadbed?

Q. I mean the ties and plates.

A. That is correct.

Q. They would be worn a good deal. In the next place, if there hasn't been any depreciation on your road, as compared to a new road, when your ties are not new, when the plates are worn, and the rails half worn out—

A. One day after you built a new road it would be different than when you built it, and—

Q. I know that—

A. —one year after you built it it would be different than what it was when you built it.

Q. I know that, but I am asking you if there is any depreciation in the elements that make up the roadbed.

A. Certainly.

Q. You didn't take any depreciation in making this up of any kind, did you?

A. That is correct.

Q. Let us take up the question of equipment. You said that in the case of equipment you took the cost of the equipment new less depreciation, did you not?

A. Yes.

Q. What depreciation rules or orders did you follow in taking that depreciation?

A. I determined the per cent of depreciation used by the Bureau of Valuation in making their element of value for December 31, 1935, and used that same per cent, condition per cent, which was based on observation at that time by the Interstate Commerce Commission.

Q. You mean that the Interstate Commerce Commission in Washington observed this railroad, observed every car on it?

A. They came out and made an inspection. That was their—

Q. How long did it take to make that inspection?

[fol. 1273] A. Oh, it was a matter of several weeks.

Q. You know that the Interstate Commerce Commission changed its rates of depreciation in 1935, and again in 1938, didn't they?

A. That is correct.

Q. Well, a good deal of this equipment runs way back of 1935 and 1938, doesn't it?

A. It does, yes, sir.

Q. Now, is it not a fact that the rate of depreciation established by the Commission and used by the Bureau of Valuation in 1935 and 1938 not only provided for the depreciation of the equipment during the remaining life of the equipment, but also undertook to provide for setting up a depreciation, which, over the remaining life of the equipment, would wipe out the deficiency depreciation on account of charging too low rates before that date? Do I make myself clear? It is a little involved.

A. I am not familiar with their procedure in that respect.

Q. Then you don't know whether the depreciation you put in here is actual depreciation or whether it is a rate of depreciation which anticipates ten years of use before the depreciation is really covered, do you?

A. It certainly looked to me like a very low condition per cent, but considering the age of some of our equipment, it looked like it was about right.

Q. That is what you put down, you just considered the age, and in general it looked all right to you?

A. I took it as a starting point, because they had made an inspection, and I presumed—

Q. But you didn't take into consideration the orders of the Commission directing the method by which depreci- [fol. 1274] ation should be charged, which undertakes to take up over a period of years in the future deficiency depreciation in the past? You didn't take that into consideration at all, did you?

A. No.

Q. Now, let me ask you, did you take into consideration the functional obsolescence of this equipment?

A. I have no doubt but what it was taken into consideration by the Bureau, and I simply followed their figures.

Q. You didn't yourself, and you don't know if they took it into consideration, do you?

A. Yes, I am quite sure they did.

Q. How do you know they took it into consideration? Just how do you know?

A. Because of a number of arguments I had with them over equipment. According to their theory, it wouldn't be in existence, but it was still running, and I know their theory of depreciation of equipment takes it into account.

Q. I am talking about not the physical depreciation of equipment, in which they set up an arbitrary rule that the equipment would be retired in so many years by use. That doesn't always work out. I am not talking about that. I am talking about functional obsolescence, which is something the Interstate Commerce Commission doesn't always figure, if it ever does, on equipment.

A. I don't—

Mr. Wood: I would like to object to the question, on the ground that there has been no testimony here as to what functional obsolescence is. Without such testimony I think the question is improper.

Mr. Anderson: I assumed that everybody here knows [fol. 1275] what functional obsolescence is. You may have a 30-ton car that is no longer useful for the service of the railroad. It may be in perfectly good condition, but

functionally obsolescence makes it useless to the railroad.

A. switch may be in perfectly good condition, but on account of putting in heavier tracks, functional obsolescence makes it useless. I thought everybody here knew the meaning of functional obsolescence. I explained the meaning, and I will be glad to put an expert on the stand to explain it further.

Q. You know what I am talking about, don't you, Mr. Lightburn?

A. Yes, sir.

Mr. Wood: There has been no testimony about how much equipment, if any equipment, is functionally obsolete.

Mr. Anderson: I didn't say it was. I asked the question whether or not it had been taken into consideration?

Q. You answered that you did not take it into consideration?

A. That is correct.

Q. Now, in arriving at the value of the equipment, assuming as you say you did, that the ICC formula applies, what did you do beyond applying the formula to that equipment?

A. I studied our costs of extraordinary equipment maintenance for the past five years and determined that there had been a considerable excess cost of maintenance put into the equipment, that should bring it up, and I added that excess money spent for maintenance to bring the value that I had fixed because of depreciation up to where I thought it ought to be.

Q. Well, but your excess costs of maintenance alone only overcome deficiency and maintenance before that, won't it?

A. Yes.

[fol. 1276] Q. Why did you add an additional value, if the property was properly maintained? A valueless depreciation is what you have here.

A. I was trying to arrive at the approximate condition per cent.

Q. You sat in your office and valued that equipment on those formulas you described, did you?

A. Yes, sir.

Q. You didn't personally inspect that equipment, did you?

A. I did not.

Q. Those figures you set up here are your theoretical figures arrived at by taking the ICC figures, which you assumed to be correct, and then coming to the—not inspecting the property at all, and adding to the value of the increased cost of maintenance which recently accrued, is that correct?

A. That is it.

Q. All right. Let us take some of these items that you say ought to be added after your exhausted the ICC figures, as I understand it, as referred to on your Exhibit No. 5. What about these telegraph lines? Who owned them?

A. The Western Union Telegraph Company.

Q. How long have they owned them?

A. Since 1917.

Q. 1917?

A. Yes.

Q. Well, you put down here telegraph lines as part of the property of the Debtor. You are talking about telegraph lines, things that the Western Union owned?

A. No, not exactly that. We claim and contend that we enjoy and possess an easement on those lines, by reason of the fact that we gave them to the telegraph company under certain circumstances, and had retained the right to have wire space on the poles.

[fol. 1277] Q. Isn't that the right of every railroad under every Western Union contract in existence?

A. I imagine——

Q. As far as you know?

A. Yes, sir.

Q. Isn't that something you pay for and charge whatever it costs and charge it to operating expense?

A. No, we don't charge it to operating expenses.

Q. Isn't your telegraph contract part of your operating expense?

A. No, but this thing I am talking about is an equity that we actually paid for. We bought it, and it was in our capital account at one time.

Q. But is out now?

A. Yes.

Q. The I. C. C. wouldn't let you put it back in there, would they?

A. No.

Q. Yet you put in $300,000 for something you don't own, the I. C. C. wouldn't let you use as capital, just a contract right to use the telegraph lines?

A. Yes, sir.

Q. How long does the contract run?

A. I couldn't tell you; I don't remember.

Q. Yet you valued it, not knowing how long it would run? It might expire next week?

A. I assume that any extension would give us the same right we have now.

Q. You wouldn't undertake to ask this Court to find a value on that assumption, would you, that you could get the same kind of contract when it expired?

A. No, I wouldn't.

Mr. Hodges: I object to that question, that he could get the same sort of contract.

Mr. Anderson: I stand by the witness' statement.

Mr. Hodges: You put the words in the witness' mouth.

[fol. 1278] Mr. Anderson: On cross-examination I have a right to put words in the witness' mouth.

Mr. Hodges: Not if they are untrue. I don't know how they do it in Virginia.

Mr. Anderson: They do it right in Virginia.

Q. Now, let us take up water rights. Describe those water rights a little more fully, will you?

A. There are two parts to that figure there. The first part is what we contend our water rights are worth, the water rights that we have to take water from streams and springs and from other sources and use in our locomotives.

Q. Do you pay anything for the right to take that water out of springs and streams?

A. In some cases we bought them and paid substantial amounts for them, in most——

Q. I mean do you pay anything currently?

A. No.

Q. Are they carried in your capital account?

A. Well, those that we paid money for certainly are.

Q. How many of those did you pay money for, and how much?

A. I haven't the figures here.

Q. How did you arrive at $465,000, if you don't know what you had in the capital account, what you paid for them?

A. Just in the same manner we arrived at the value of our lands, by comparing them with the right to use the

same amount of water at any place where we knew the value of the water.

Q. Do you have to pay for that water currently by the year, or rent it?

A. No, sir.

Q. Just your right to take water out of a stream or river or spring, for which you in many cases paid nothing, but [fol. 1279] acquired it probably by use, and in other cases you bought it, and you don't know how much you bought. You haven't valued them on the ground, you just put down $465,000 as representing their value, is that right?

A. No, part of that figure that we claim for water rights is about $150,000, and I have in my files full support of that figure, based upon the worth of water rights in the country that we traverse.

Q. You don't know whether the I. C. C. ever allowed you to put them in your capital account or not, do you?

A. I said I was quite sure that some of it wasn't in the capital account. Wherever we bought ditch rights, water rights, they are certainly in the capital account.

Q. $150,000. Where is the balance? The balance of your claim was disallowed by the Bureau of Valuation.

A. We claim that we should have irrigated land value where we went through irrigated lands, and they gave us a value of lands without water rights, and we knew that under the reproduction theory, if we went through irrigated lands, we pay irrigated land prices for the water rights.

Q. How do you arrive at the value?

A. I have explained that, just on the basis of their admitted value of irrigated lands.

Q. But the value was not allowed in the valuation of the I. C. C.

A. That is correct.

Q. You took the valuation of the I. C. C. when it suited you and added to it when it didn't, is that the idea?

A. No, I followed the valuation theory pretty closely.

Q. Well, now, these can-on rights, $3,180,000, is that allowed by the I. C. C.?

[fol. 1280] A. No, that is an amount in excess of the nominal land value that they allowed when they appraised our land.

Q. How did you arrive at the value of those can-on rights?

A. It has been a long time ago that those figures were made, at least ten years ago, and I don't recollect exactly how we did it, but they are an appraisal, an honest appraisal, to buy them at that time.

Q. Understand I am not questioning your integrity at all. I am merely trying to get the facts. But the figures were made ten years ago. You don't remember exactly how they were made or how they were arrived at, or the basis on which they are arrived at, but you put them in here as a value which you ask the Court to accept; is that correct?

A. Yes, because I thought it was correct for the reason that most of these canyons where we did possess valuable rights, do today, we fought for them in the early days.

Q. I know you did.

A. The value of similar adjacent lands was somewhere in the way of two or three dollars an acre that the Interstate Commerce Commission allowed.

Q. I know. You fought for them, but you wouldn't say that the fact that you had quite a battle to get them from another railroad establishes a value for them in the market?

A. Well, I believe I would say that it did.

Q. Would you say you could fix a value for that, how many men were killed, or how much blood was shed?

A. No, that wasn't the basis.

Q. Now, the efficiency and value of mortgage equipment, I wish you would explain that, will you?

A. I wonder if I could read my manuscript here at the same time?

[fol. 1281] Q. Yes, I didn't get it.

A. At the time of the valuation inventory the Rio Grande owned 3,258 units of narrow gauge freight cars, of which 2,767, or eighty-five per cent, were purchased during the ten years immediately preceding the valuation date. Having been purchased so near to the valuation date, it was considered that the original cost of this equipment was a better measure of value than any hypothetical figure set up by the Bureau as of 1910-1914 price level. This position is also emphasized by the fact that the price per unit to this carrier in almost all cases increased after the valuation date. We actually found out what that difference was.

Q. In other words, your valuation of that equipment, as I understand it, is in excess of the original cost as ascertained by the Interstate Commerce Commission?

A. No, it was their cost of reproduction, I think.

Q. Well, whatever their method was, it was in excess of the original cost?

A. I am not talking about original cost. I am talking about the cost of reproduction.

Q. Well, cost of reproduction.

A. That gave us substantially less than we paid for the equipment.

Q. As of 1930, have you depreciated it at all?

A. Oh, yes, indeed.

Q. At what rate? I mean under what order? I am not asking you to state the percentage.

A. As I said before, I took their computation of per cent based upon the whole equipment account.

Q. But that would be an order of determination which led to absorption, forming depreciation and depreciation [fol. 1282] charges. If you say that, you are carrying in the value of the equipment a depreciation which has not been absorbed; isn't that correct?

A. I don't believe we are talking about the same thing. This observed condition per cent has no relation to any of their depreciation for equipment. In the last three years, in making up this cost of reproduction, I used the book depreciation which I presumed was based on those Interstate Commerce Commission rates.

Q. And you took all the balance as being the present value of the equipment regardless of whether that had been reached in depreciation before that order, or not?

A. I just merely took their observed condition per cent as a straight——

Q. Now, the cost of development of property, not to take too much time, on what theory did you undertake to add into the value of the property the original cost of its development, having valued the property itself upon the basis of cost of reproduction new? Will you explain that to us?

A. On what theory?

Q. Yes.

A. The theory that the carrier would be entitled to that certainly in a rate base.

Q. I am not talking about rates now. I am talking about reorganization.

Mr. Hodges: Let him answer your question.

Mr. Anderson: He said certainly on a rate base they were entitled to it. Now, I am not talking about a rate basis here.

Q. Well, you said you thought they were entitled to it. Was that the only reason you put it in there?

A. Yes, sir.

[fol. 1283] Q. That is the only basis you have for that $9,000,000 item?

A. Well, I didn't just pick it out of the air. That figure was testified to in our primary valuation hearing before the Commission, and it is my recollection that the figure was made up by our Treasurer and our Auditor as their best estimate of what should be in there.

Q. But you have no knowledge of your own as to the correctness of those figures?

A. I haven't, no.

Q. And you are not accurate in your memory as to what the testimony was, are you?

A. I haven't reviewed the testimony.

Q. When did that testimony take place?

A. 1926.

Q. Fourteen years ago. Now, the going concern value, if you allow for cost of development of property which creates the going concern situation, do you add a going concern value to that also?

A. I did. I think you should.

Q. Well, if the cost of development of $9,000,000 creates its going concern condition, and you take that cost in as a part of the value of the property, on what do you base the going concern value in addition to that?

Mr. Hodges: I object to that. The theory of the cost of development is not that the cost of development takes in the going concern value.

Mr. Anderson: If the witness wants to correct it he can correct it. If my question does not put it fairly he can correct it.

Mr. Hodges: I can correct it.

Q. Unless the Court desires otherwise, you can answer the question.

[fol. 1284] The Court: He may answer.

A. I would like to have the question read.

Q. (Question read to the witness.)

A. I testified in direct testimony and gave a rather lengthy set of reasons for this cost of development of physical property and also for going concern value. I feel that they are different matters entirely. They both belong in the valuation.

Q. Not to prolong the discussion, the development of business you feel is not included in the development of property? That is a proper matter of establishing relationships, etc.?

A. Yes, sir.

Q. Aren't those relationships the good will of the property, going concern value, and good will?

A. Well, we estimated them all separately in making our claim.

Q. How did you arrive at the value of that, Mr. Lightburn?

A. As I recall it, we had our officers pass their opinion on what that element was worth.

Q. Well, have you anything on the subject yourself?

A. It is the very definite opinion that development of business costs you something.

Q. Yourself, have you ever had any experience in the development of traffic of a railroad?

A. Oh, not as a traffic officer, but I have been certainly where I could see it.

Q. Well, now, suppose that the earnings of this property a year, instead of being $23,000,000, were $18,000,000. Would you change your valuation in any respect of the property?

A. Well, I did change it from the original claim that we made in the 19A valuation here. We claimed $26,500,000.

[fol. 1285] Q. I am not speaking of that. You misunderstood me. I have now left that item. And, taking your valuation as a whole, let us say that the earnings of this property, instead of $23,000,000, were $18,000,000; would that change your valuation of the property in any way?

A. No, not if the property had been physically maintained in the condition we assumed it to be on our original valuation. The difference of whether it was carrying $23,000,000 worth of business or $18,000,000 wouldn't make any difference in value.

Q. And if it was $5,000,000 your answer would be the same, wouldn't it?

A. Unless the condition at the time we reduced the earnings to $5,000,000 affected the price trend and other figures I used in making this valuation.

Q. Assuming that the price of commodities and other elements entering here were the same, your valuation would be the same if it earned $5,000,000?

A. Yes, sir.

Q. And it would be the same if it earned $40,000,000, wouldn't it?

A. Yes.

Q. Or $50,000,000?

A. That is right.

Q. And you would say that the value of this property was what you have stated here without any regard whatever to what it would earn, or what return it would pay on any valuation you established; is that correct?

A. That is correct. That was the approach we made to it.

The Court: Mr. Hodges, are you trying to determine the value of this property?

Mr. Hodges: I am trying to determine the value of the property.

The Court: Aren't you bound by the Interstate Com-[fol. 1286] merce Commission under the law?

Mr. Hodges: No, not at all, but even under the statute you have before you, Section 77, the testimony which we have introduced is testimony made relevant by that statute if it had no other relevancy. I will argue that at the proper time. In fact, Congress nor any other party——

The Court: Apparently the language here says that is binding upon the Court. Did they certify a value here?

Mr. Hodges: If that is what the statute means and if that is the view adopted by the Court, for that reason it clearly violates the constitution of the United States—clearly so. This Court has the duty of determining the value of this property. I will furnish the Court with all the information and testimony we can produce.

The Court: In that language it seems to me that valuation certified by the Commission is binding upon the Court. The question arises——

Mr. Hodges: They have not certified any value here.

The Court: We should refer it back and ask them to do it.

Mr. Hodges: I think it would be a futile thing to ask them to do, because it is a responsibility that the Court

must take, and the Congress cannot take that responsibility or duty away from the Court in a proceeding of this kind. It is entirely different from any matters we have met up with in later years where in controversy of proceedings an administrative body is given power to find a value and their findings are made binding upon the Court. This is based on a different theory and resting straight and [fol. 1287] squarely upon the constitution. I am prepared to argue that when the time comes.

The Court: Mr. Clay, do you want to examine the witness?

Mr. Clay: Yes, sir, I have several questions.

By Mr. Clay:

Q. Mr. Lighthurn, I understood that various of these exhibits have been prepared by you substantially in accordance with the methods used by the I. C. C. Did I understand you correctly?

A. Yes, sir.

Q Would you briefly describe what those methods are? Who does the work?

A. I attempted to do that in my direct testimony; but I will be glad to go over it again for you. The I. C. C. valuation of carrier properties, including this, is based, as you know, upon the inventory. Quantities were inventoried in the field. Quantities of all kinds, except the land and the equipment, were determined by this field inventory of the engineer.

Q. They are employes of the I. C. C.?

A. They are employes of the I. C. C.

Q. But their work is not official, is it, until it is acted upon by the Commission?

A. It was a joint inventory. We had representatives with them. They did the actual engineering work.

Q. Isn't it true that these various employes of the I. C. C. made an investigation to determine what they call the factors of value?

A. Elements of value.

Q. Isn't it also true that only the I. C. C. itself makes the valuation and determination?

A. No, that is not true.

[fol. 1288] Q. In which they give here to these factors?

A. No, up to a certain point it is a joint affair. We agree with them.

Q. You agree with whom?

A. With the representatives of the Bureau of Valuation.

Q. With the Commissioners?

A. Certainly.

Q. It is an agreement with the Interstate Commerce Commission?

A. This land appraisal that we made in 1937 was a joint appraisal. We had a representative and they had one, and went over the ground.

Q. And found the new values, and changed the old values?

A. And made a new——

Q. Now, Mr. Lightburn, aren't you enough familiar with the ICC practice to know that the ICC alone makes the determination of value?

A. I understood that, but as to these elements of value and the things that you get when you go out in the field to make examinations, etc., a certain amount of that information is jointly agreed to, and it is common property.

Q. It is merely information for the Commission, isn't it?

A. Well, that is what we used in fixing my valuations.

Q. Information as to the elements of valuation?

A. That is correct.

Q. Is that upon the valuation by the ICC for rate making of this property?

A. Not since 1919. They determined and published some data on elements of valuation dated——

Q. Who published it?

A. The Interstate Commerce Commission.

Q. You mean the employes?

[fol. 1289] A. Pertaining to this case. And this is prima facie evidence in this reorganization case in 1937.

Q. But with your familiarity with methods of valuation for rate making by the Interstate Commerce Commission, isn't it true that after this information has been prepared by the employees it is considered by the full Commission, and the Commission gives one weight to one element, and another to another, and arrives at what they call a single valuation?

A. Yes, we did that in 1919. They haven't done it subsequent. In this case the Commission itself doesn't certify any final value.

Q. There has been no final valuation by the Interstate Commerce Commission?

A. That is correct. They just submitted some elements of valuation.

Q. Colonel Anderson referred to what he called functional obsolescence of the equipment. Isn't it common knowledge that there is also functional obsolescence of roadbed because of these motor trucks and buses?

A. Well, it might be conceded, but we don't concede it in the railroad business until the time comes for us to abandon a branch, and then I guess they would.

Q. In other words, you haven't given any consideration to functional obsolescence of plant due to increase of your competitors' inroads on your business?

A. Not in this valuation.

Q. The Trustees of the Rio Grande Western I believe have pending a petition to abandon the line in New Mexico, the line from Alamosa to Santa Fe?

A. That is correct.

Q. Can you tell me what value you placed on that line in this valuation, roughly? Was it either $5,000,000 or $10,000,000?

[fol. 1290] A. I am sorry that I have not present with me——

Q. Can you give any estimate of approximate range?

A. Of the value of that line?

Q. Yes.

A. I could in a few minutes by referring to my data.

Q. Does it run into millions?

A. Yes, it would be probably more than $2,000,000.

Q. More than $2,000,000?

A. I should think.

Q. If you have the figure there I would be glad if you would——

A. I haven't it here. I could get it. I had it when I made up the figures. I had it in my office.

Q. You put that line in at full value even though you know the Trustees are trying to get permission to abandon it?

A. Yes, I put the line in at full value.

Q. Have you put the various narrow gauge lines in at their full value although some of them may be approaching the point that that line last referred to has?

A. Yes, I put them in at full value, but I don't believe that many miles of our narrow gauge system are in that state at the present time.

Q. Now, in case you get permission from the Court and the Interstate Commerce Commission to abandon this line from Alamosa to Santa Fe, can you give me an idea, based on your own experience as to what the salvage value will be?

A. Yes, I can give you——

Mr. McAllister: It is not from Alamosa. It is from Antonito.

Mr. Clay: I stand corrected. I believe the two points [fol. 1291] are not far apart, are they?

Mr. McAllister: Antonito is some distance south of Alamosa.

Mr. Clay: Not more than twenty miles, is it?

Mr. McAllister: Well, I don't know. The line from Alamosa to Antonito is not to be abandoned.

Mr. Clay: It is the southern line to Santa Fe.

Mr. McAllister: Yes.

Q. Suppose this line you valued at $2,000,000 is abandoned?

A. Let's not use the $2,000,000 figure.

Q. What will be realized by the Trustees from the abandonment?

A. Well, a very small part of that amount. Just the salvaged rail and bridge timbers, etc., would only amount to——

Q. Would it be one-fiftieth of the amount?

A. I think it would be more than that.

Q. Or perhaps one twenty-fifth?

A. A good many thousand dollars, yes.

Q. As much as $100,000?

A. No, I don't think it would be that much.

Mr. Clay: That is all I have.

Mr. McAllister: May I ask one or two questions for the Trustees, and I want it understood that I am not appearing in a partisan spirit. I simply want to bring out some facts.

By Mr. McAllister:

Q. Mr. Lightburn, I think this first question I will ask has been fully covered by Colonel Anderson's questions, but it was in my mind before he cross-examined. This testi- [fol. 1292] mony you have given about cost new and cost

less depreciation all has to do with the physical cost of the property based thereon, the physical value of the property?

A. That is correct.

Q. And, putting the matter in a little different form from the way Colonel Anderson put it, it wouldn't make any difference with respect to the values as to which you have testified, as to whether the net earnings were zero or five or six million dollars, or even more than that; is that correct?

A. None whatever, unless as I said to him, the condition that made the lack of business also affected the price level.

Q. Well, you mean affected the costs of material and labor?

A. That is correct.

Q. Now, I call your attention to Debtor's Exhibit 4, dealing with the Denver and Salt Lake Western Railroad Company. I had a great deal to do with borrowing money from Reconstruction Finance Corporation to build that line. That is the Dotsero Cut-off, is it not?

A. It is.

Q. It is my recollection that we borrowed from Reconstruction Finance Corporation—the Rio Grande did—$3,631,000 to cover the complete cost of the line. If it cost more than that I think perhaps we missed a bet, because I thought we were borrowing all we could to build that line, but you have the cost of reproduction new of that line in Debtor's Exhibit 4, four million five hundred and ninety-seven thousand odd dollars, with land values of $12,000.00 added. Is it correct that the original cost of that property in 1934 was about $3,631,000?

A. Very close to that amount. I have the cost up to [fol. 1293] December, 1935, of $3,547,000.

Q. What is the reason for the greatly increased cost of reproduction new which you have shown in Debtor's Exhibit 4?

A. The very sudden and rapid rise of construction costs, beginning just about 1934 and going right up to near the end of 1937.

Q. Well, then, during that period, construction costs must have gone up about twenty-five per cent?

A. They did generally. The cost of grading did not go up, but other construction costs did go up very materially.

Q. Well, then, that answer explains the reasons for your figures in Debtor's Exhibit 4?

A. That is right.

Q. Colonel Anderson asked you something about the valuation you placed on water rights. Have water rights a recognized value in Colorado?

A. They certainly have.

Q. And also in Utah?

A. Yes, sir.

Q. The doctrine of appropriation applies in those states, does it not?

A. It does.

Q. And the first appropriator has the best water right, generally speaking?

A. That is correct.

Q. And such water rights are bought and sold, are they?

A. Bought and sold just the same as any other real property.

Q. And in the case of the Rio Grande certain of these——

By the Court:

Q. Are these decreed water rights you are talking about?

A. Yes, sir.

Mr. James A. Marsh: Are they irrigation water rights?

Mr. McAllister: Yes.

[fol. 1294] By Mr. McAllister:

Q. You purchased some?

A. Purchased some or appropriated or filed on others. That doesn't decrease their value.

Q. Those rights have been recognized as belonging to the Rio Grande?

A. They have been adjudicated and decreed.

Q. Adjudicated and decreed water rights do you consider have a fairly fixed value?

A. I do.

Q. And it is upon your information with respect to that value or those values that you have valued the water rights mentioned in Debtor's Exhibit 5?

A. It is, sir.

Q. Mr. Lightburn, are you familiar with a report of the Bureau of Valuation of the Interstate Commerce Commission as of December 31, 1935, affecting all of the companies embraced in Debtor's system, which was filed by that Bureau of Valuation with the Commission at its request?

A. I think I have seen that, Mr. McAllister, but I——

Mr. Hodges: May it please the Court, I wish to make an objection to references to that Bureau of Valuation elements of value which was filed before the Interstate Commerce Commission. We make the objection so that I will not, as a consequence of failing to make an objection, make competent as evidence that report. That report was filed, and all parties—well, I can't say all parties, but Colonel Anderson's group and ourselves and I am sure some of the others joined—objected to the introduction of that document called elements of value, for reasons fully set forth in the record. The objection, of course, was overruled, and the elements of value are referred to by the ICC in their report. I wish to [fol. 1295] protect our position that those elements of value as filed by the Interstate Commerce Commission were no evidence there, and they are no evidence here. They were just filed. They are not such a document or statement as authorized to be filed under Section 77, and to be made prima facie evidence of facts recited. Those elements of value are not statements of fact from our point of view, and are not authorized by the statute, and are not competent evidence. It may be quite enlightening to see them and know what they are, but I don't want to be prejudiced here or hereafter by any technicality in regard to the matter, and by allowing, without objection, interrogation to be made which might bring them in as part of the record properly and without objection. So I do object to referring to these so-called elements of valuation filed by the Bureau of Valuation, not under oath, and not under the authority of Section 77.

The Court: You say they are in the record?

Mr. Hodges: They are in the record here. They are certified here, but our objections are also filed with them.

The Court: Is this cross-examination?

Mr. McAllister: This is cross-examination, but I think I will let it rest on that, because the report is in the record of this court, and, of course, can be referred to along with all other parts of the record.

Mr. Anderson: I think the objections made to evidence continue in this court and can be availed of at the proper time. I assume that is true upon the record in the de novo [fol. 1296] hearing. We did object to those so-called elements of value, because they are not a valuation, and they

didn't do anything, and therefore we want to insist upon our objection to them, but we will not argue them.

Mr. McAllister: I think you are correct that proceedings before the Commission may be considered by this Court subject to the objections you make.

Mr. Anderson: Yes, of course.

Mr. McAllister: I won't ask for an answer to that question.

The Court: Is that all?

Mr. Wood: Your Honor please, I would like to ask four or five questions following along with the questions Colonel Anderson asked.

By Mr. Wood:

Q. Mr. Lightburn, these exhibits of valuation which you put in state value at December 31, 1938, do they not?

A. They do.

Q. At December 31, 1938, what was the average age of the rails on the standard gauge lines of The Denver & Rio Grande Western Railroad Company?

A. I haven't the exact figure. I know that the property generally was in very good physical condition.

Q. Do you know approximately what the average age of those rails was?

A. I haven't that information with me.

Q. Can you get that figure so that we can put it in the record here?

A. I think so.

Q. Can you tell me also what the average age of the narrow gauge rails was at the same date?

[fol. 1297] A. I would just be guessing if I tried to give it to you. I get it.

Q. Will you please get that figure?

A. Yes.

Q. What is the approximate average life of the standard gauge rails?

A. It depends entirely on the place you put them.

Q. Well, let us take the approximate average life of standard gauge rails on main lines.

A. About ten years.

Q. About ten years?

A. Yes, under the heaviest traffic. From ten to twenty years. We have rails on our track that have been in forty

years with the same traffic going over it. We would not allow rails that old to stay in with the speedy traffic.

Q. Those old rails that you speak of are on branch lines or where the traffic is light?

A. No; we have rails that are over forty years old on our main track; they are not where there is high speed; they are at the end of the yard or some terminal. When I say ten years' life of rail, I do not mean that the rail is worn out in ten years, but we might take it and put it somewhere else at the end of ten years.

Q. But if you take it out it means that you have to replace it with new rails?

A. That is correct, but we might put it somewhere else to keep from buying new rails, by putting it somewhere else.

Q. What is the approximate average life of the narrow gauge rails?

A. Oh, forty years, probably. You mean how long it stays in before we have to remove it?

Q. That is right. At December 31,1938, what was the average age of the standard gauge ties?

A. I haven't that information with me. It is all available in our engineering department, but I did not come prepared [fol. 1298] to answer questions of that kind.

Q. Can you get that figure so that we could have it put into the record?

A. Yes, I think so.

Q. And also could you get the average age of the narrow gauge ties?

A. Yes, sir.

Q. And what is the average life of the standard gauge ties?

Q. Twenty-five or thirty years.

Q. What is the average life of the narrow gauge ties?

A. You asked me about that.

Q. No, I asked you about the standard gauge ties.

A. It depends on whether they are treated or untreated, and it depends entirely upon the place they are, the amount of traffic that is going over them, and on whether they are in a curved territory, and so on. We have no——

Q. I realize that it depends on the place where they are used, but, obviously, what I am trying to get at here is the comparison between the average age of these types of property on December 31, 1938, and the average life, and if we

can get those figures, that comparison should show something even though we all understand that the average life is different depending on where the use is.

A. Well, first let me correct that answer I gave you on the average life of standard gauge ties. I thought you asked about the narrow gauge. I know the standard gauge average tie life is less than twenty years, and the narrow gauge is less than thirty years.

Q. Well, is it not true that a new railroad would require no new rail for perhaps twenty-five years, or not much new [fol. 1299] rail, and would require no new ties for perhaps twenty years?

A. No, that is not true. If you think about the Rio Grande now—my first answer about that rail is correct; in the heavy traffic we would not dare to leave it as long as we would any other place; we would certainly not leave ties in a track for twenty years in that traffic.

Q. What percentage of the standard gauge rail would you estimate, approximately, on those heavy density lines, that gets the hard use, that has to be very frequently replaced?

A. Well, there isn't such a very large percentage of them in the heavy curved territory.

Q. Ten per cent?

A. Yes, it would be that much probably.

Q. Not much more?

A. There wouldn't be any more than that.

Q. It is true, is it not, that bridges wear out—bridges and trestles wear out just like rails and ties?

A. Unless they are properly maintained. We have bridges that have been there since some of our narrow gauge lines were originally built, by replacing timbers, that are still there; the character of the traffic hasn't changed, but they are in a place where there isn't heavy traffic. Am I answering your question?

Q. I think you are. It is true, is it not, if you have a wooden bridge, the timbers of which have expended half their life, that you have the same result as though the bridge was half worn out, because instead of building a new bridge to replace the old one you would merely substitute timbers?

A. That is right.

Q. But the bridge has in effect used up half its life under the circumstances that I state?

[fol. 1300] A. Well, so far as the question of its value is concerned, you can say that its life is diminished, but so far as its serviceability is concerned it is still one hundred per cent, and by keeping it so, it will keep on going indefinitely. If the piles rot off we drive new ones, or with the timbered bridge, if the stringers wear out—and we determine that by regular inspection—we simply put new timbers in, and it is charged to operating expense. So the value of the bridge is there and it is just as serviceable until you have to change it for some other reason.

Q. But if the timber were new you wouldn't have to expend any money to speak of on the bridge until the timbers had become old, would you?

A. No.

Q. It is true, is it not, that the elements of value of the Bureau of Valuation of the Interstate Commerce Commission do give effect to depreciation in structural right of way of the kind that I have been mentioning, namely, the age of the rails and the ties and the bridges and the trestles?

A. Yes, that is the way the Interstate Commerce Commission Bureau of Valuation determines it.

Mr Wood: That is all.

(Short recess.)

Cross-examination.

By Mr. Fitzgibbon:

Q. Mr. Lightburn, in your Exhibit 7 is an allocation of equipment valuation among various mortgages, are you expressing any opinion as to the lien of the mortgages upon equipment?

A. No; I testified that we were just trying, with all the information we had, to allocate it approximately; we do not [fol. 1301] pretend to say which equipment belongs to which mortgage.

Q. And what you did as you took an agreement between a certain limited number of parties to this case as of 1935, you got certain percentages from that and then brought those into your 1938 date?

A. Yes. But in addition to that we made an adjustment—approximate adjustment—of what we had learned from the agreement; some of the bondholding interests shifted some

of that equipment from the Refunding and Improvement to the D. & R. G. Consolidated.

Q. Do you know what the original cost of this equipment was new as shown on the carrier's books, with additions and betterments to the end of 1938?

A. Yes. I just took the 1935, recorded our original costs and added the net additions to equipment for the three succeeding years, and find it to be $48,496,901.

Q. In the Commission's elements of value what was the figure that they took for this equipment new?

A. You mean cost of reproduction new or——

Q. Cost of reproduction new, yes.

A. They used the 1935 cost of reproduction new, $50,179,822.

Q. Now, Mr. Lightburn, what I understand you did—and correct me if I am wrong—you took the Commission's reproduction new, with additions and betterments, and you took certain index figures to arrive at a different cost, and with that result you then got to your figure of 68 million some odd?

A. $68,661,095 for the value of equipment as of December 31, 1935.

Q. And to that figure of 68 million you then applied [fol. 1302] depreciation figures which were approved by the Commission in their order of 1938—that is, you reject the Commission's valuation; you reject—I grant it solely for this purpose—you reject the original cost as shown by the carrier's books; you reject the Commission's basis of some 50 odd million, yet you do accept the Commission's depreciation rates?

A. Yes, because they were made after at least a cursory examination of the equipment and it was their best judgment of the condition and it came not very far from what was on our books.

Q. But the Commission was applying those to a different base?

A. They were applying them to a different base.

Q. And various elements go into fixing a depreciation rate, and one of them would be the original cost, would it not?

A. I don't believe they took any account of the original cost in making their estimate of cost of reproduction less depreciation.

Q. I am not using depreciation in that sense. I am talking about when you fix a certain valuation for property that might have a very strong relation to your depreciation rate.

A. Well, I don't believe——

Q. That is the same element that Colonel Anderson has previously spoken about: If you feel that your valuation is high you will fix one rate; if your valuation is low you might fix another rate; it does, of course, depend on the expected life still to run?

A. Well, I don't know that I can just answer your question. Would you——

Q. Well, I am really making an observation, and I am asking you to address yourself to that, as to why you feel justified in taking the Commission's depreciation rate and [fol. 1393] rejecting their base figure.

A. Their base figure, according to our view of the way it was arrived at, was manifestly wrong. I had access to their pricing data and knew where their so-called 1935 price level was, and it was nowhere near where it should be for the subsequent period, that is, the period of 1938.

Q. Then you disagree with the thought or the proposition that if equipment has been insufficiently depreciated in the opinion of one body, that you should not take then a higher depreciation figure for the remaining life of the equipment?

A. Let me see if I understand you,——

Q. Let me rephrase the question: Assume that the equipment is on the books at $1200 and you believe the value of that equipment is $1,000, if you keep the base figure of $1200, assuming a ten-year life in each case, won't you take a higher depreciation figure if you leave $1200 on the books rather than if you leave $1000 on the books?

A. Yes, certainly.

Mr. Fitzgibbon: That is all.

Redirect examination.

By Mr. Goree:

Q. Colonel Anderson asked you about canon rights of way. I want to inquire whether this was a pure conjecture on your part, that is, the value of some three million several hundred thousand dollars that you assigned to these canon

rights of way, or if you had some actual experience upon which to base this value?

A. It is my recollection that in arriving at this figure which was computed by our chief engineer, that the value of that occupancy—the canon—was related to what it would cost us if some other railroad had been there ahead of us [fol. 1304] and we had to build on the other side of the canon, let us say.

Q. Well, what canon do you have particularly in mind, now?

A. Of course, the striking example is the Royal Gorge. We have track on one side of the Royal Gorge and at one time we made complete surveys and a very careful estimate for double-tracking that stretch of our road through the gorge, and we had before us, when these estimates of canon values were computed, the excess cost of that second line over on the other side of the canon. Likewise, we had actual cost figures of construction of our second track through the Eagle River canon. That was actually constructed. We knew the cost of the first line and we knew the cost of the second line on the other side of the canon and took the difference, and by numerous computations and data of that kind we arrived at this figure of three million odd dollars for canon rights in excess of the amount that had been allowed by the Commission based on similar adjacent land which was nothing but grazing lands.

* * * * * * *

[fol. 1305] WITNESS WILLIAM WYER

My first exhibit deals with the question of the historical effect of the opening of the cut-off on the volume of the Rio Grande's transcontinental freight traffic. This exhibit is in two sheets.

Mr. Anderson: Group Exhibit No. 1, or I think probably Committee Exhibit No. 1 would be better.

(The paper presented was marked for identification Committee Exhibit No. 1.)

The Witness: There are two sheets. The first one is marked Sheet 1.

This exhibit is headed "Transcontinental Freight Traffic Estimated Tons of Principal Commodities Handled by Various Transcontinental Carriers, 1928-1939, Inclusive."

All of the figures shown on here are in tons except certain figures which are obviously in percentages, and the three zeros have been omitted, so all of the figures represent thousands of tons. All of the figures on here are taken from annual reports of the various carriers to the Inter-
[fol. 1306] state Commerce Commission for the years shown, and the exact figure which has been taken from those reports is indicated in the table at the bottom of Sheet 1. The exhibit shows the tonnage of a number of different commodities of transcontinental freight for all of the principal transcontinental railroads of the country. These are the Denver and Rio Grande Western, the Union Pacific, the Atchison, Topeka & Santa Fe, the Great Northern, the Northern Pacific, and the Pacific Lines of the Southern Pacific.

Mr. Clay: May I ask a question at this point?

By Mr. Clay:

Q. This exhibit is headed: "Estimated Tons of Principal Commodities." Will you explain how you made these estimates?

A. I will do that in the course of my——

Q. Before you go any further.

A. I will do it at the proper place. I do not think this is quite the place to go into the detail basis——

By the Court:

Q. As I understand it, this column 1 here is actual figures that these roads actually handled?

A. These are actual figures taken from the annual reports of these railroads to the Interstate Commerce Commission.

Q. In other words, the Denver and Rio Grande handled east only 800 tons of oranges and grapefruit?

A. Eight thousand tons.

Q. How many tons to a carload?

A. That would be about 500 cars, I should think, or a little more.

Mr. Clay: I object. Did Mr. Wyer make this estimate? Who made the estimate? He has not testified.

[fol. 1307] The Court: The Witness stated he did.

The Witness: I expect to explain in detail just how the estimate was arrived at, but there is an orderly way of

making the explanation, and I prefer to follow the orderly way.

Mr. Clay: There is an orderly way to explain the basis before you give the testimony in the record.

Mr. Anderson: Your Honor please, I desire to have this witness give all the information possible to the Court and counsel on this subject, but I think if we start cutting it up and breaking it up with all kinds of intervening questions it will simply confuse, and counsel will have abundant opportunity to cross-examine after the primary situation has been presented in order, and while I do not wish to offer any restriction on the counsel I hope they will refrain from interrupting the development of the case, and that they will make their notes and ask the questions when it is their time.

The Court: I think that is the proper procedure. Go ahead, Mr. Wyer.

The Witness: I haven't made any figures on this for the Western Pacific which is largely a transcontinental railroad, but the reason for that is that all of the tonnage handled by the Western Pacific is delivered to one of the railroads that is shown on this exhibit, that is, either the Denver and Rio Grande Western or the Union Pacific or the Great Northern, so that if the Western Pacific's tonnage were included it would simply be a duplication of totals shown under other railroads, and one of the purposes of this study is to show the proportion of the total trans-conti- [fol. 1308] nental traffic of this country which the Rio Grande has handled during the period covered by this exhibit. Having shown the roads which I show on this exhibit, I then show the principal transcontinental commodities in which the Rio Grande is interested. These are by no means all the commodities which are handled by the Rio Grande or by these other railroads, and they do not include absolutely all the business handled by the Rio Grande as transcontinental business, but they include all the commodities which are predominantly transcontinental in so far as the Rio Grande is concerned. The annual report of the Rio Grande to the Interstate Commerce Commission shows its commodities in four classifications. The first of these classifications is business originating on the Rio Grande and terminating on the Rio Grande. Obviously that is not transcontinental business. The second classification is business originating on the Rio Grande, but delivered to connections. Now, the maximum possible haul that such business could

have would be if it originated at Ogden and moved east, and was delivered to a connection at Denver, or vice versa, but that also would not be transcontinental business. The third classification which the Rio Grande reported to the Interstate Commerce Commission is business received from connections and terminating on line, and that obviously cannot be transcontinental business, because it terminates at some point on the Rio Grande. And the fourth classification which the Rio Grande reports to the Interstate Commerce Commission is business received from connections and delivered to connections, and that, equally obviously, is [fol. 1309] almost entirely transcontinental business. The only business included in Class 4 which would not be transcontinental would be small amounts which the Rio Grande might receive from a short line connection such as a central route. Also if business originated on the Western Pacific, we will say, just west of Salt Lake City, that might not be considered transcontinental business, although as far as the Cut-off is concerned it is competitive, and it is really transcontinental. So that fourth classification is almost exclusively the transcontinental business of the Rio Grande, and there is not any other transcontinental business included in any other classification. So I started by taking the commodities of the Rio Grande, which, according to the report to the Interstate Commerce Commission, were important transcontinental commodities, and then I took for each of the other carriers the figure from this annual report to the Interstate Commerce Commission which most closely approximated its handling of the same commodities in transcontinental movement, and the total at the bottom of Sheet 1 shows exactly which classifications I took for each of the other carriers. Because of the different situation of those carriers, that classification is always not the same, or I should say not always the same as Class 4, which I took for the Rio Grande, but practically the classification which in my opinion gives the closest approximate to the transcontinental tonnage for each of these commodities for each of the other railroads. Now, the Rio Grande's principal competitor for transcontinental business is, of course, the Union Pacific, so that my first comparison which I made [fol. 1310] from this exhibit was to compare the Rio Grande's transcontinental business with the total transcontinental business of the Rio Grande and the Union Pacific combined. I might explain that a little further in this way: that there

are three main transcontinental routes: the northern route served by the Great Northern and the Northern Pacific; the central route served by the Union Pacific and the Rio Grande; and the southern route served by the Southern Pacific and the Santa Fe. The Santa Fe also competes somewhat for central route business, and the Union Pacific competes somewhat for southern and northern route business. The Great Northern competes somewhat for central route business, but, by and large, they are the three main routes, and the different competitors on each of those routes are as I have stated. So that the first comparison is to show what percentage of the central route transcontinental traffic was handled by the Rio Grande in each of these years, and I show those percentages in the bottom quarter of Sheet 1 of Exhibit 1. I show them for each particular class of traffic, and then up in the right-hand column I show them for the total, and you will notice that in 1928 the Rio Grande handled 16.4 per cent of the total transcontinental traffic of the central route, and that in 1939——

By the Court:

Q. Where does that appear?

A. That appears on Sheet 1 in the right-hand column, the first figure in the fourth big block. The block is described; "Percent D&RGW to total D&RGW and UP," and the per [fol. 1311] cent is the first percentage in the right-hand column.

Q. In other words, the Denver and Rio Grande handled 16.4 per cent of all of this on the central route?

A. Yes, sir, in 1928, and in 1939 its percentage of the central route business had increased to 25.4 per cent.

Q. You say over here "Percent D&RGW to total D&RGW and UP."

A. That is correct.

Q. In other words, of the total business handled by those two routes, the Rio Grande handled sixteen per cent?

A. Sixteen per cent in 1928, yes, sir. In other words, the total business handled by those two roads less the transcontinental business handled by the central route.

Q. That went up to twenty-five per cent in 1939?

A. That is true. Now, in connection with those percentages I would like to point out that the Dotsero Cut-off was opened for business on June 15, 1934, and that from

1928 to 1933 the Rio Grande's percentage of the transcontinental traffic on the central route increased from 16.4 to 22.2, or 5.8 per cent of the total business of that route. From 1934 to 1939 the increase was from 22.2 per cent to 25.4 per cent, or only 3.2 per cent of the total business on the central route. In other words, the Rio Grande's gain in comparative position in the handling of transcontinental traffic over the southern route increased more in the five years prior to the opening of the Dotsero Cut-off than it increased in the five years subsequent to the opening of the Dotsero Cut-off. That is a tremendously basic fact, and it is important to keep it in mind all through this consideration of the Dotsero Cut-off which I am going to [fol. 1312] make in my study. Now, on Sheet 2 of this exhibit I make the same comparison for all transcontinental traffic in the country. That comparison is found in the bottom block on Sheet 2, where I show "Percent D&RGW to total all lines." In 1928 that was 4.5 per cent. That is, the Rio Grande was handling four and a half per cent of all the transcontinental business of the country in 1928. In 1939 that had increased to 7.4 per cent. Now, making that same comparison of the five years prior to the opening of the Cut-off with the five years subsequent to the opening of the Cut-off, we find that from 1928 to 1933 the Rio Grande's proportion of the total transcontinental business of the country increased from four and a half per cent to 6.2 per cent, while from 1934 to 1939 it increased from 6.3 per cent to 7.4 per cent, so that the increase during the five years prior to the opening of the Cut-off was 1.7 per cent of all the transcontinental business of the country, and the increase in the five years after the opening of the Cut-off was 1.1 per cent of the total of the business of the country, so that if you make the comparison on the basis of the business of the central route, or whether you make it on the basis of the total transcontinental business of the country, the Rio Grande's proportion grew more in the five years prior to the opening of the Cut-off than it grew after the Cut-off opening.

* * * * * * * *

[fol. 1313] Mr. Anderson: I offer the exhibit described by the witness as "The Denver and Salt Lake Railway Company Account" as Committee Exhibit No. 19.

[fol. 1314] The Court: It will be admitted.

August 3, 1940

Mr. Anderson: I now offer the printed reports of the Trustees for the D. & R. G. W. for 1937, 1938 and 1939. By the way, I have not given numbers to the others, so I will now ask leave to give. The reports of the Denver and Salt Lake for 1937 I ask be received and marked Committee Exhibit No. 21. The report of The Denver and Salt Lake Railroad Company, annual report, for the year 1938 I ask be received in evidence as Committee Exhibit No. 22. The report of The Denver and Salt Lake Railway Company for the year 1939 I ask be received in evidence as Committee Exhibit No. 23. I now offer in evidence report of The Denver and Rio Grande Western Railroad Company, Wilson McCarthy and Henry Swan, Trustees, for the year ended [fol. 1315] December 31, 1937, and ask that it be received in evidence as Committee Exhibit No. 24. A similar report of the Trustees of the D. & R. G. W. Railroad for the year ended December 31, 1938, and ask that it be received in evidence as Committee Exhibit No. 25. A similar report of the Trustees of the D. & R. G. Railroad Company for the year 1939, and ask it be received in evidence as Committee Exhibit No. 26.

[fol. 1316] By the Court:

Q. This Debtor's plan you have been discussing calls for total fixed charges including preferred stock of $7,768,000. Have they ever had earnings available in any year of that amount?

A. Yes, they had in 1928, 1929 and 1930, earnings in excess of that.

[fol. 1317] Q. You mean the consolidated property?

A. Yes, sir.

Mr. Anderson: May I ask a question?

The Court: Yes.

By Mr. Anderson:

Q. When you speak of fixed charges, don't you mean fixed charges of the capital fund, contingent interest and preferred stock?

A. Those are hardly fixed charges. Those are total cash requirements for the service of those securities.

Q. Is that the $7,000,000 you refer to?

A. The $7,768,000 would take care of all the interest, both fixed and contingent, and all the preferred stock, dividends, and the capital fund and sinking fund.

Q. That is what I thought; I wanted to make it clear that that was not fixed charges.

A. That is correct, that is not the fixed charge, the fixed charge is only $2,538,000.

Mr. Hodges: I notice the Court's question referring to fixed charges incorporated the bonds and preferred stock as part of the fixed charges. I just want to call attention to that, because of course that is not a fixed charge.

The Court: I mean, your total charges on your structure here calling for $7,768,000. Is it your opinion that that can be earned, based upon past history?

The Witness [William Wyer]: I think you would find sometimes when that would be earned; it would not be earned very often, but I think you would find a year now and then when that figure would be reached.

Of course, there is one thing that is a matter of technical accounting, which I think ought to be considered in connec-
[fol. 1318] tion with that matter of charges, and that is that under the Interstate Commerce Commission classification that capital fund and your sinking funds are not charges against income. That is, that goes to reduce your debt, but they will go to add to your assets, and they are not charges against income under the Commission's classification of accounts. If you took those items out you would be taking out slightly over a million dollars.

By the Court:

Q. What are those items?

A. The sinking fund and the capital fund, those two items amount to just a little bit over $1,000,000, so that if you take them out, your actual interest and dividends on the securities outstanding is reduced to about $6,760,000.

Q. If you take them out there is in sufficient earnings to support your plan to carry out all the provisions you have here?

A. Taking them out would not change the amount of the earnings, it is simply a matter, as I say, of how you state

the charges against your income, and under the Commission's classification, those representing investment of new money or retirement of debt, are not charges against the income of the company.

Q. You mean, the sinking fund is not?

A. No, sir, it is not.

Q. Don't you believe a sound financial plan would require a sinking fund?

A. Yes, I think it ought to be in the plan and we have it in our plan, but I am simply saying on the basis of the Commission's regulations, that would not be a deduction from your income.

[fol. 1319] Q. I understand that, but you say this financial structure has been supported by the earnings, that is, to the extent of the fixed charges, but not paying anything on the stock?

A. What I tried to say was that on the average since the last receivership these fixed charges have been covered; I am not certain whether the charges including capital fund and sinking fund have been covered or not. I would like to check that up and give you the exact figure, but in the three years 1928, 1929 and 1930, all of the charges, including interest on the preferred stock and the capital fund and the sinking funds, were covered by earnings, and there has been income available for that in those three years.

Q. What is that capital fund to be used for; what is the nature of it?

A. It can be used for anything in the way of adding to the property or improving the property that the management may decide to use it for.

The Court: That is all I have to ask.

By Mr. Hodges:

Q. The Court asked one question and got an answer there that I do not quite understand, and I would like to clear it up. In order to do that I have to make a statement. Prior to 1932 you have a history of earnings of this Debtor Railroad since the Salt Lake Cut-off, and possibly extending prior to that time, which would support the structure which we propose. Since 1932, under conditions prevailing in this country, the earnings of this property have dropped to a lower level, and to date you have before you that picture. Did you intend to say that in the tomor-

row, or would you attempt to say, that this road would [fol. 1320] earn enough to carry the structure you propose, in some years, but not with regularity? Now, I understood you to say to the Court that in the future, from what we know today, we could simply say that the structure you propose could be carried out in some years, but the implication lies at least, not with regularity. Do you undertake to say that?

A. What I believe about that situation is this: First, let me say I did not make any estimates of my own as to future earnings on this property. We rely on the estimates made by Mr. Pyeatt and Col. Ayres, and what I am saying is based upon their studies. Based upon their studies, the fixed charge of $2,538,000 would be safely earned. The total, including contingent interest of $4,343,000, would be more than earned on the average, but there would be years when it would not be earned. The total of $7,768,000, including the preferred stock, would be earned occasionally, but not very often.

Q. Do you understand that the earnings which they projected were the maximum earnings that could be expected from the railroad?

A. No, I do not understand their estimates to be maximum earnings.

Q. They figured that amount by normal years, did they not?

A. Yes, I think they define that in some detail.

Q. And, in short, it was that within a reasonable time we could be expected to be back to that level of earnings?

A. As an average; there would be some years it would be below it and some years it would be above it.

Q. Didn't they define their normal year as that year that we might be expected to reach when some of the adverse [fol. 1321] conditions which now surround this road—and perhaps the industry—ceased to operate to the disadvantage of the road?

A. Yes.

Q. And they did not attempt to say that that was the top to be expected, nor did they encourage us to expect to return to the earning conditions which preceded the depression?

A. I think that is correct.

By the Court:

Q. That was for 1939; wasn't it, which they adopted as the normal year?

A. I think there was some time, and that they hoped that that condition would arrive by 1939.

Q. Didn't they give estimated earnings for 1939 as the typical year?

A. No, we did not give an estimate for 1939; they gave this estimate what they expected to be normal earnings, and then I think that they said that they hoped that that situation would develop by 1939.

Q. Have those earnings ever been made by this property?

A. You mean, since they made the estimate, or prior to that time?

Q. At any time.

A. Yes, they have been made in a good many years prior to the time they made the estimate. I think Mr. Pyeatt's estimate was around $6,000,000, maybe a little bit more.

Q. What?

A. About $6,000,000, as I recall it.

Mr. Anderson: If I may state to the witness, $6,215,423 was Mr. Pyeatt's estimate of net in a normal year.

The Witness: $6,215,000?

Mr. Anderson: Yes.

[fol. 1322] The Witness: Estimated gross.

By the Court:

Q. Have those figures ever been reached in any year?

A. They were reached in 1927, when the figure was $7,300,000; 1928, when it was about $8,600,000; 1929, when it was $10,350,000; 1930, $8,000,000. 1931 almost reached it, $6,100,000. I have not got the figures here for 1925 and 1926, but I think they were also in excess of that figure.

Mr. Anderson: Your Honor will understand in repeating the figures to the witness I am not adopting that testimony, merely stating the figures.

By the Court:

Q. What was the depreciation and maintenance that year? Didn't those figures go down a good deal?

A. You mean, included in Mr. Pyeatt's estimate or in those years?

Q. In those years you speak of, in reaching those figures.

A. I think for those years the maintenance was pretty high. In 1927, 1928 and 1929, they were high; the property was carrying on a very heavy improvement program. Now, the maintenance in 1925 and 1926 was pretty low as to equipment, because in those years, under special authority from the Interstate Commerce Commission, the road was charging the cost of rehabilitating its equipment, taken over at the end of the receivership, to capital account, and was not charging a good deal of maintenance of equipment, which under ordinary circumstances would have been chargeable that way. During the entire period I think the depreciation charges were probably a little lower than they should have been. I would say in 1927, 1928 and 1929 [fol. 1323] maintenance and depreciation charges were fully adequate. In 1925 I would say they were too low for normal expenditure.

Q. When the property came into the court in 1935 hadn't the maintenance been unusually low?

A. I think for probably two years prior to that time they had been held down pretty low.

Q. It was not maintained, then?

A. I think there was some cut in maintenance in 1935 and 1936.

By Mr. Hodges:

Q. Was that condition of cut in maintenance peculiar to this road or not?

A. No, that is a condition that I think you will probably find on any road that is struggling to maintain itself—its financial life. I have had occasion to make studies of railroads that have gone into bankruptcy, just from that point of view, and I think it is a common characteristic you find in nearly every road that goes into bankruptcy, that at the time it goes in there exists some need of maintenance, because the management has been struggling to keep afloat.

Q. Have you made any study to find out the condition with respect to need of maintenance of other Western roads that were not struggling to keep their heads above water, say, during that period of low business?

A. I think that was generally true; in fact, I know it was generally true of most railroads in the country during that period.

Q. And it is true in that period of low business, and this threat, whatever it was, the tendency of all railroad managements, and particularly those in the West, was to curtail their maintenance expenditures?

[fol. 1324] A. I do not think it was confined to railroads in the West; I think you might say that that was true of railroads generally, and particularly true of railroads whose financial condition was threatened.

By Mr. McAlister:

Q. Mr. Wyer, from your study, is it not evident that one reason for undermaintenance during, say, two or three years prior to 1935, was due to the desire to keep up the interest upon the funded debt of the Debtor?

A. Yes, I think that is correct.

By the Court:

Q. Was there some interest paid that was not earned? Have you any figures on that?

A. Yes. I think during the year 1934 there was probably some interest paid that was not earned. I think that was the year that occurred. Possibly 1933, also.

By Mr. Hodges:

Q. Can you call the Court's attention to an exhibit which you prepared, showing the years in which certain payments could have been made on deferred dividends on common stock, in which the money was reinvested in the property? You remember the exhibit?

A. Yes, I remember the exhibit.

Q. Do you have the number of it?

A. No, I do not.

Mr. Hodges: We will supply your Honor with the number of that exhibit.

By Mr. McAllister:

Q. It was true, as to provisions in the general mortgage, that the interest upon the general mortgage bonds would not become a positive, fixed, charge until 1929, and

[fol. 1325] that, speaking generally, that prior to that time the directors had power to utilize the money instead of paying that interest upon the property, in order to keep it a going concern?

A. It was due in part to that, but the exhibit which I prepared and put in the case showed what would have been available for the preferred stock, and I think, in three years, for the common stock, if all the arrears on the general mortgage had been made up, either way.

By Mr. Marsh:

Q. Did your exhibit show the application of the arrears?

A. I think it did, Mr. Marsh.

Q. That was one of the matters that was briefed before the Commission?

A. In fact, it showed in each year the making up of all arrears and what would have been available if the arrears up to that time had been made up. It did not anticipate future arrears, but I think it made up all past arrears.

Q. Well, the exhibit will show?

A. The exhibit will shew, but I am pretty sure the basis covered all past arrears on general mortgage bonds.

The Court: That is all I care to ask the witness. Do any of you gentlemen care to examine him further?

By Mr. Anderson:

Q. Mr. Wyer, there were some questions asked by the Court and also by counsel as to the improvement program before the period of bankruptcy. Do you know, from your investigation of the property and from the various reports here, whether there has been some extended improvement program since the period of bankruptcy?

[fol. 1326] A. Yes, there has been a very heavy program.

Q. The annual reports of the Trustees are in the record, and they give, with reasonable accuracy, the results of those and their effect upon maintenance of way charges and their effect upon other factors involved, do they not?

A. Yes, they do; and I have a special statement here which gives that effect quite accurately.

Q. Will you give that?

Mr. Anderson: I want to clear this question up. We will rely on it, because it is an important question in the

argument of this case. I might say the Commission recognized the effect of the maintenance and life improvement program, whether in bankruptcy or in the operation of the company.

Mr. Clay: That is discussed in the Commission's record, pages 5105 and 5106.

Mr. Anderson: But I want to get the facts on the record here.

A. In the four years, 1936 to 1939, which, of course, are all within the period of trusteeship, the charges to operating expenses in connection with additions and betterments, including additions and betterments on leased lines, were as follows: 1936, $1,118,842. 1937, $1,972,284. 1938, $742,820. 1939, $1,272,409.

Mr. Clay: May I ask Mr. Wyer where he got those figures? Is that a Trustee's statement?

The Witness: Those are taken from the statement prepared by the Accounting Department dated May 17, 1940, headed "Charges by Classes to Operating Expenses in [fol. 1327] Connection with Additions and Betterments, including those on leased lines, for the following periods."

Mr. Clay: Well, is that as it came from the Trustees' staff, or have you readjusted it?

The Witness: No, there are no readjustments on that.

The Court: Will you turn to page 5104 of the printed record? What do you say in regard to those figures there on the amount of fixed interest charges, $2,774,554?

The Witness: That is the figure that the Insurance Group Committee, I believe, considered was the safe fixed charge. That is the figure they thought was a safe fixed charge.

The Court: What?

The Witness: A safe fixed charge. That corresponds to the figure that the Debtor thought was a safe fixed charge, around 2½ million.

The Court: Do you think these figurse are correct, then?

The Witness: Well, we did not differ very much from the Insurance Group Committee as to what a safe fixed charge should be. They figured about 10 per cent higher than we did. I think our figure of around 2½ million is still correct.

The Court: They arrive at $2,774,554 as the allowable amount of fixed charges. Do you agree with that?

The Witness: I think it ought to be a little lower. As I say, in our Debtor's plan, we had a figure a little lower

than that. We made the fixed charge as much as we thought [fol. 1328] could be safely carried, and there isn't very much between us, but I think my figure is a little lower than that. Understand, that is not any figure of earnings —that is simply the opinion of the Insurance Group Committee as to what the fixed charge should be, safely.

* * * * * * *

[fol. 1329] Thereupon, the Guaranty Trust Company, to maintain the issues herein in their behalf, offered and gave evidence as follows:

T. A. THOMPSON, called by the Guaranty Trust Company, being first duly sworn, testified as follows:

Direct examination.

By Mr. Fitzgibbon:

(Thereupon a document was marked for identification as Guaranty Trust Company Exhibit No. 1.)

Q. Mr. Thompson, I show you a statement marked Guaranty Trust Company Exhibit No. 1 for identification. Will you state what that is?

[fol. 1330] A. It represents a statement of payments by The Denver and Rio Grande Western Railroad Company to the Denver and Salt Lake Railway in connection with the joint operations over the lines of the Denver and Salt Lake between Utah Junction and Orestod, for the calendar years 1936, 1937, 1938 and 1939.

Q. That correctly reflects the payments made by the Denver to the Denver and Salt Lake during the period indicated by you, as shown by the books of the bankruptcy Trustees?

A. It does.

Mr. Fitzgibbon: I ask that that statement be received, Your Honor.

The Court: Any objection? (No response.) If not, it will be admitted.

Mr. Fitzgibbon: Your Honor, will you give counsel a moment to look at it?

(Thereupon documents were marked for identification as Guaranty Trust Company Exhibit No. 2.)

Mr. Clay: May I ask counsel what this is? Are these the figures on the operation by the D. & R. G. W., or the payments made to the Denver and Salt Lake in connection with that operation—the trackage contract and the lease of the D. & S. L. W.?

Mr. Fitzgibbon: I will ask that question of Mr. Thompson.

The Witness: It represents all payments by the Rio Grande to the Denver and Salt Lake Railroad under its trackage contract between Utah Junction and Orestod.

Mr. Clay: Does that include the unusual payments because of the program on the D. & S. L.?

[fol. 1331] The Witness: Yes, sir.

Mr. Clay: It is all the payments by the D. & R. G. W. to the Denver and Salt Lake?

The Witness: It is all the payments by the D. & R. G. W. to the Denver and Salt Lake under that trackage contract.

Mr. Clay: Have there been any other payments?

The Witness: There are some supplemental agreements that cover expenditures east of Utah Junction. They are inconsequential, but, nevertheless, there have been payments.

By Mr. Fitzgibbon:

Q. Those are the payments on the basis stated by you, shown in your accounting office?

A. They are.

Mr. Fitzgibbon: I might proceed, your Honor, with another exhibit, if you will withhold the ruling on Guaranty Exhibit 1.

The Court: There have not been any objections yet?

Mr. Fitzgibbon: None as yet.

The Court: Very well.

Q. What are the so-called Copeland density charts?

A. The firm of Copeland and Son, of New York, each year secure from the Rio Grande, and I believe from most of the railroads throughout the country, figures showing information as to the net and gross ton miles passing over the various parts of those railroads.

Q. I have handed you Guaranty Trust Company Exhibit No. 1 for identification, which purports to show the traffic density for the years 1935 to 1939. Have those totals that I have handed you been checked by you?

A. They have.

[fol. 1332] Q. Are those tables somewhat similar to the charts which were offered as Debtor's Exhibits 21 to 21-D and 105 before the Interstate Commerce Commission?

A. They show the same information.

Q. Except that the exhibits before the Commission were in chart form and yours are in table form?

A. That is correct.

Q. On that table that I have handed you is a reference in the upper right-hand corner to east density and west density. What does that mean?

A. It refers to the density of traffic eastbound which, in the case of the Rio Garnde, means toward Denver or Pueblo, and Westbound away from Denver and Pueblo. It refers to the density of traffic in gross ton miles and includes the equipment net ton miles load only.

Q. And those figures have been obtained from the books of the bankruptcy Trustees?

A. They have.

Q. On these tables that I have handed you there have been several calculations made, have there not?

A. Yes.

Q. Have you checked those calculations?

A. I have.

Q. Those calculations are to reduce the ton miles to average tons per mile, are they not?

A. That is correct.

Q. And those calculations are correct?

A. They are.

Mr. Fitzgibbon: I would like to have the statement received as Guaranty Exhibit 2. I think, in order for purposes later on in connection with briefing, we might have the table for 1935 referred to as 2-A; the table for 1936 referred to as 2-B; for 1937, 2-C; for 1938, 2-D; and for 1939, 2-E.

[fol. 1333] Mr. Fitzgibbon: Your Honor, I now offer Guaranty Exhibit 1 and Guaranty Exhibit 2-A to 2-E, inclusive.

The Court: Any objection? (No response.) It will be admitted.

* * * * * * *

[fol. 1334] August 7, 1940

Mr. Fitzgibbon: May it please the Court, there was circulated last week among the necessary parties to this proceeding certain supplemental information as to the Utah Fuel Company. The entire stock of that company is placed under the Western Consol Mortgage. There being no objection, I should like to offer these as Guaranty Trust Company's exhibits. I think it might be well that they be embodied in one exhibit of six sheets. Inasmuch as Exhibit 3 has not been offered and I have had no request—that is the branch line report—I would ask that there be received in evidence as Guaranty Trust Exhibit 3, Sheet 1, a letter dated July 19, 1940, of Mr. Moroni Heiner, President of the Utah Fuel Company, to Mr. Arthur E. Burke; as Guaranty Trust Company Exhibit 3, Sheet 2, a statement dated July 19, 1940 of Castle Gate Costs for the Period January 1 through June 30, 1940, and 1939, and Comparison; as Guaranty Trust Exhibit 3, Sheet 3, statement dated July 19, 1940, entitled Utah Fuel Company and Subsidiary Companies Summaries of Consolidated Income, Years Ended December 31, 1933, Through 1939; as Guaranty Trust Company Exhibit 3, Sheet 4, statement dated July 19, 1940, entitled Utah Fuel Company and Subsidiary Companies Condensed Balance Sheets—By Companies and Consolidated—At December 31, 1939; and as Guaranty Trust Company Exhibit 3, Sheet 5, a statement dated July 19, 1940, entitled Utah Fuel Company and Subsidiary Companies Condensed Balance Sheets—By Companies and Consolidation, December 31, 1933; and as Guaranty Trust Company Exhibit 3, Sheet 6, a statement dated July 18, 1940, entitled Utah Fule Company adn Subsidiary Com-
[fol. 1335] panies—Summaries of Income and Profit and Loss by Companies for the Period, January 1, 1940, Through June 30, 1940, and Summaries of Consolidated Income Through June 30, 1940, and 1939, And Comparison.

The Court: You have three exhibits here altogether?

Mr. Fitzgibbon: One exhibit with six sheets to it.

The Court: Any objection? If not, it will be admitted.

By Mr. Fitzgibbon:

Q. Mr. Thompson, I show you Guaranty Trust Company Exhibit No. 5, marked for identification. Will you please state what that is?

A. It shows the traffic density on the Denver and Salt Lake Western and the Denver and Salt Lake Railway, the movement on the Denver and Salt Lake Western being entirely by the D. & R. G. W., and on the Denver and Salt Lake as to the joint line, by the D. & R. G. W. and the Denver and Salt Lake; and on the non-joint Denver and Salt Lake, by the Denver and Salt Lake exclusively.

Q. This was prepared pursuant to a request that was made after the introduction of Guaranty Trust Company Exhibits 2-A to 2-E, inclusive, was it not?

A. That is correct.

Q. How would you get the figure for the combined operation over the Denver and Salt Lake?

A. You would simply add the joint line figures as to the D. & R. G. W. and the Denver and Salt Lake together.

Q. And that would be because the mileage remains the same, and you would not need any——

[fol. 1336] A. The Denver and Salt Lake and the Denver and Rio Grande ton-miles are figured on exactly the same mileage; therefore, you would just add them together.

Mr. Fitzgibbon: This is Guaranty Trust Company Exhibit No. 5. The title, reading it into the record, is "Net Tons (Revenue and Company) per Mile of Road, D. & S. L.-W. R. R., D. & S. L. Ry." and endorsed at the bottom, "Accounting Department, August 6, 1940."

The Court: Would you explain what that means?

The Witness: That means that the average movement over the Dotsero Cut-off proper, from Bond to Orestod, involves a total of 126,000 net tons. That does not include the car in which the load was moving, nor any movement of empties.

The Court: It means the revenue received?

The Witness: No; it does include the company's.

The Court: What proportion is the company's?

The Witness: Well, I would just have to estimate that, your Honor. I would say 10 per cent—less than 10 per cent.

The Court: Ten per cent?

The Witness: The approximate figure would be pretty close to the difference between the 772,000 and the 826,000.

Mr. Fitzgibbon: I would like to ask that this be received as Guaranty Trust Company Exhibit No. 5.

The Court: If there is no objection, it will be admitted.

(Guaranty Trust Company Exhibit 5 accompanies this record.)

[fol. 1337] Witness William Wyer

Q. Well, doesn't your answer merely illustrate the weakness of the D&RGW in competing for this transcontinental traffic? It only has a short haul and has to compete with highly competitive business; isn't that true?

A. I think it does, and that is one reason why I think you are about in the peak in your proportion of transcontinental traffic, as I have testified.

Q. That is, you are not very optimistic about the future of the D&RGW?

A. I don't think its proportion of the total will grow very much more. I think it will keep its place as to total gross.

Q. That is, the proportion of the total business of the Denver and Rio Grande Western to other groups?

A. The proportion of the transcontinental business of [fol. 1338] the Rio Grande Western to the total transcontinental of the country.

[fol. 1339] Witness C. M. Lightburn:

Mr. Wood: If Your Honor please, if it were the conven-[fol. 1340] ient way to proceed, I have some questions to ask Mr. Lightburn on an entirely different subject. On the first day of the hearing here, on cross-examination, I asked Mr. Lightburn, at pages 90 to 92 of the transcript, to obtain certain information regarding the average age and the average life of rails and ties on the D&RGW system. Mr. Lightburn has been very cooperative in trying to obtain the information which we requested, but it has not been found practicable to supply the information in exactly the form in which we requested it. However, we are prepared, through Mr. Lightburn and through another witness, whom we shall call subsequently, to present such information as is readily available on the subject referred to, and if it is convenient that we should go ahead with that now, I am prepared to do so.

The Court: All right.

(Thereupon a document was marked for identification as R&I Trustees' Exhibit No. 7.)

By Mr. Wood:

Q. Mr. Lightburn, I show you a statement entitled, "Gross Tons Rail Purchased, Including Dotsero Cutoff," showing the tons of new rail and second-hand rail purchased, for each of the years 1920 to 1940, inclusive, and ask you whether you prepared this statement, and whether the figures shown thereon are correct.

A. I prepared the statement, and the figures are correct.

By The Court:

Q. In 1922 you bought 21,000 second-hand rails? Is that correct?

A. Yes, sir, it is.

[fol. 1341] Q. And that is what was used on the Denver and Salt Lake Western?

A. No, Your Honor; that was used on narrow gauge main lines.

Q. This says second-hand rail, including the cutoff.

A. Yes, but this does not show that. It shows all rail purchased for renewals.

Q. Purchased for renewals?

A. Yes.

Q. Why do you say, then, "Including Dotsero Cutoff"?

A. Any renewals that were made on the cutoff are included in here, but not the original construction rail.

By Mr. Wood:

Q. Mr. Lightburn, adding up the figures shown in the second column, under the heading "New Rail," what is the total number of tons of new rail purchased during the years 1920 to 1940, inclusive, as shown on the statement?

A. 205,456 gross tons.

Q. And the total amount of second-hand rail shown is 26,932 tons, is it not?

A. That is correct.

Q. Do you know the total number of tons of rail in all lines of the D. & R. G. W., including also the cutoff line from Dotsero to Bond?

A. It was approximately 426,333 tons.

Q. Referring to the statement showing the gross tons of rail purchased during the 21 years 1920 to 1940, inclusive, will you please state what percentage of the total amount of new rail purchased during that period, being the figure which you gave, 205,456 tons, is to the total amount of all rail in the tracks of the D. & R. G. System, including the cutoff line from Dotsero to Bond?

A. It is approximately 48 per cent.

Mr. Wood: I offer the statement entitled, "Gross Tons [fol. 1342] Rail Purchased, Including Dotsero Cutoff" in evidence as R. and I. Trustees' Exhibit No. 7.

Mr. Anderson: I do not know what counsel's purpose is in introducing the evidence, but it does not show the weight of rail; it does not give any indication of miles of new rail; it may be 50-pound rail or 100-pound rail, or any other pound rail, and therefore gives us no idea to go on. If they have that information and propose to offer it later, it might be interesting, but I don't know what it would be interesting on to give how many tons of rail he bought.

Mr. Wood: We have a later exhibit which we are going to put in through another witness which I think will go a long way toward supplying the deficiency that is referred to.

Mr. Anderson: I object to this because it does not prove anything. He might just as well introduce a book of songs as this.

Mr. Wood: The exhibit is offered in evidence.

The Court: It will be admitted.

(R. and I. Trustees' Exhibit No. 7 accompanies this record.)

By the Court:

Q. All the rail bought by the Trustees in the last three or four years, set forth on this statement, would have been 112-pound rail, or higher?

A. 112 and 130-pound rail.

Mr. Wood: I might repeat what I said: We recognize here that the direct answers to the rather simple questions which we asked on the first day apparently could not be [fol. 1343] given, and so what we are doing here is to give what Mr. Lightburn and the other witness, whom we will present, considered to be the best information available, and is not exactly what we would have wished to put in if we could have obtained the answers to our questions.

By Mr. Wood:

Q. Mr. Lightburn, I now show you a statement entitled, "Tie Renewals and Estimated Total Ties in Track, Including Dotsero Cutoff," showing the tie renewals for the years 1919 to 1939, inclusive, sub-divided as between standard gauge ties and narrow gauge ties, and further sub-divided to show the numbers of untreated ties and treated ties. Did you prepare this statement, and are the figures shown thereon correct?

A. Yes, sir.

Q. I note that the statement shows, for the years 1923 to 1939, inclusive, the estimated total number of ties in all tracks, both standard gauge and narrow gauge. Will you please supplement the statement by telling us approximately how many ties which are included in the total figures are ties in the Dotsero cutoff line from Dotsero to Bond?

A. About 142,000.

By the Court:

Q. According to this estimate, you have got less ties in the road now than you have had for several years; is that right?

A. That is correct.

Q. Is that due to abandonment?

A. To abandonment of branch lines.

Q. You have a lot less mileage, then?

A. Yes, sir.

Q. What percentage of this estimated total ties has been [fol. 1344] relaid?

A. Approximately 90 per cent.

By Mr. Wood:

Q. The percentage figures in column 8 on the right-hand side of the statement show, do they not, for each year, the percentage which the amount of tie renewals during the year bears to the total estimated number of all ties in the track?

A. They do.

Q. If the percentage figures shown for the years 1925 to 1939, inclusive, are totalled, does it not appear that the number of ties relaid subsequent to 1924 is 103.34 per cent of the total number estimated to be in the tracks?

A. That is correct.

Q. On the basis of the figures shown on the statement, have you made an estimate of the average age at the present time of the ties in the tracks of the D. & R. G. W., including the cut-off line from Dotsero to Bond?

A. Yes. I have estimated that the average age is 9.21 years.

Mr. Wood: I now offer in evidence as R. and I. Trustees' Exhibit No. 8 the statement entitled, "Tie Renewals and Estimated Total Ties in Track, Including Dotsero Cutoff."

That is all that we have with this witness on this subject. The remainder of what we wish to put in on this subject will be put in through another witness, who will be ready immediately after lunch, at the convenience of the Court.

Mr. Anderson: Before the adjournment, may I ask a few questions of this witness?

The Court: Yes.

By Mr. Anderson:

Q. You spoke of the average age of the ties in the track. [fol. 1345] What is the average service life of treated ties on the D&RG, approximately, in this climite?

A. Our treated ties, Col. Anderson, have not been in the track long enough for us to get a historical record. We are guessing and hoping and thinking that they are going to last over 20 years on an average.

Q. Your ties are tie-plated on the line?

A. Yes, sir.

Q. Completely?

A. Completely tie-plated on the main line.

Q. Of course, you haven't the figures and experience, but you are estimating 20 years' life for the treated ties in the regular service?

A. An average on the line; possibly less on the heavy traffic lines.

Q. Of course, on curves and heavy traffic line, but the average will be about 20 years?

A. At least that.

Mr. Anderson: If Your Honor please, before I sit down, I would like to ask if counsel could not supply us with any exhibits they propose to introduce after lunch. We supplied ours well in advance of presentation. It would save us a lot of time and give us a chance to check these exhibits

if they will give them to us before cross-examination, and I will greatly appreciate it if they will do it.

(Witness excused.)

The Court: Who is your next witness, Mr. Wood?

Mr. Wood: Our next witness is Mr. Perlman. Shall we put him on now, your Honor?

The Court: Have you just a few questions?

Mr. Wood: I have only a few questions of him. Of course, I cannot say what might be asked on cross-examina-
[fol. 1346] tion, but my questions will only take a short while.

The Court: You may put him on.

A. E. PERLMAN resumed the stand for

Direct examination.

By Mr. Wood:

Q. Mr. Perlman, you heard Mr. Lightburn's testimony, have you not?

A. Yes, sir.

Q. Of the 426,333 tons of rail in the lines of the D&RGW, including the Cut-off line from Dotsero to Bond, how many tons are in the line from Dotsero to Bond?

A. There are 5,388 tons on the main line, and 2,010 tons in yard tracks and sidings, or a total of 7,398 tons.

Q. I now show you a statement entitled "Main Track Relaid or Laid with New Rail (Including that laid in turnouts) (Excluding Misc. Rail Renewals)," showing for the years 1923 to 1939, inclusive, the number of gross tons of rail laid and the number of miles of track on which such rail was laid. Did you prepare this statement, and are the figures shown thereon correct?

A. They are.

Q. The statement shows, does it not, that the average number of tons of rail laid for each year of the seventeen year period shown is, excluding the rail laid on the Dotsero Cut-off line, 10,502 tons, and that the average number of miles of track on which this rail was laid was 66.44 miles?

A. It does.

Q. What is the number of tons of rail in the main track as that term is used on the statement? That is, give the figure for the tracks, exclusive of the Cut-off line, and [fol. 1347] separate figure for the Cut-off line.

A. Exclusive of the Cut-off there are 148,697 tons. On the Dotsero Cut-off main track there is 5,388, or a total of 154,085.

Q. What is the number of miles of main track for the system, excluding the Cut-off line, and what is the number of miles of main track stated separately for the Cut-off line?

A. Our primary main track, exclusive of the Cut-off, includes 892.99 miles. The Dotsero Cut-off is 38.1 miles, or a total of 931.09.

Q. What is the average age at the present time of rail in the main track?

A. Eight and one-third years.

Q. In computing the average age did you include the average age of the rail in the Cut-off line from Dotsero to Bond, and, if so, would excluding the rail in that line slightly increase the average age for the remainder of the track?

A. I did not include the average age in the Cut-off.

Q. What do you estimate as the life of the rail in your main track, taking into account recent developments in the art of maintenance, such as building up rail ends to prolong the life of the rail?

A. Fifteen years.

Mr. Wood: I offer in evidence as R&I Trustee's Exhibit No. 9 the statement entitled "Main Track Relaid or Laid with New Rail (Including that laid in turnouts) (Excluding Misc. Rail Renewals.)"

The Court: It will be admitted.

Q. It is true, is it not, that track which is used on curves on the main line has a shorter life than the average age?

A. That is correct. The way we estimate the fifteen years, Mr. Woods, is by figuring twenty years on tangent, and an [fol. 1348] average life of ten years on curves. Some sharp curves won't last over five, and some will last fifteen, but our railroad has approximately fifty per cent of curve track and fifty per cent of tangent, and it averages out fifteen years.

Q. Yes. Well, now, as to much of this track which is used on curves on the main line, is it true that much of that

track becomes badly bent, so that when it is taken up from the main line it cannot be relaid on side tracks or secondary tracks?

A. Well, much of the heavy curvature is pre-curved for those sharp curves, so that when it is taken out of track you would get a bad curved rail to put in a tangent siding.

Q. So that in case of that type of track you cannot put it in your secondary lines after it has served its life in the main track?

A. Well, some of it is badly head worn also, and if you would put that head worn rail up against a rail that has been used in tangent, you would be liable to get derailments and have quite a bit of trouble, so that normally that rail that is taken out of heavy curves after it has served its life is scrap rail.

Q. Turning now to the subject of ties, what is your best estimate of the expected life of new untreated ties?

A. Our old records on this railroad indicate an average life of nine years for untreated ties.

Q. Mr. Lightburn said that ninety per cent of the ties were now treated. Are the remaining ten per cent of untreated ties pretty well worn out?

A. Most of them are badly decayed, and will be out within a very short time.

. . . . . .

[fol. 1349] ARTHUR RIDGWAY, called by the Debtor, being first duly sworn, testified as follows:

Direct examination.

By Mr. Goree:

Q. Your name is Arthur Ridgway?

A. Yes.

Q. How long have you worked for the Denver and Rio Grande Western Railroad and its predecessor, Mr. Ridgway?

[fol. 1350] A. Continuously for the last 45 years. Prior to that time intermittently for about eight years, I think.

Q. You are now chief engineer for the Debtor—that is, for the Trustees of the Debtor, are you?

A. Yes, sir.

Q. How long have you been chief engineer?
A. Seventeen years.
Q. Prior to that you were assistant chief engineer?
A. Yes, sir.
Q. For how long?
A. Fourteen years.
Q. Mr. Ridgway, during the time of the valuation of the properties of the Debtor, I believe you were chairman of its valuation committee?
A. That is correct.
Q. And that was a committee of some four or five or more officials of the Debtor, who had charge of this valuation work, was it?
A. I believe so. That is my recollection.
Q. Of course, Mr. Lightburn was the valuation engineer reporting to that valuation committee; is that right?
A. That is true.
Q. Mr. Ridgway, I assume you have seen Debtor's Exhibit 5, which has been introduced by the Debtor and identified by Mr. Lightburn?
A. Yes, I have seen it.
Q. I want to question you in regard to the item "Cost of Development of Property, $9,000,000." Will you tell us, please, whether the cost of reproduction new of the road accounts of the railroad company, excluding lands, correctly reflects the value of such a roadbed to a railroad company—the roadway to a railroad company?
A. No.
Q. Do you mean that there are some additional values there which are not reflected by that cost of reproduction [fol. 1351] which is determined in this hypothetical program?
A. Yes, there are additional values.
Q. Why do you say that, Mr. Ridgway?
A. Because their value accrues through time.
Q. Explain that answer, will you, please?
A. Well, if I may read my reply, instead of trying to compose it on the spur of the moment, it will be a great deal shorter.
Q. Very well.
A. The cost of reproduction new on an instant date may not exactly measure the value of an extensive and complex property when many of the parts of which it is constituted

appreciate with the lapse of time. The worth of the physical property of a particular railroad depends upon its adaptation and growth into a fitness of purpose for which it was created. There are many inseparable elements of value that accrue only through age and use. The expression of these values in monetary terms is called, for want of a better name, "the cost of physical development."

Necessity for the fitting and adaptation of the line to the natural characteristics of topography becomes apparent only through operation. Changing of line and grade and continual resurfacing and realigning of track are required before the fixed structure meets the demands of stability and uniformity for satisfactory train movement. The cost of reproduction new does not provide for this refinement nor do Road and Equipment Accounts, for its repeated expenditures are charged to Operating Expenses.

The largest single item of value of the fixed property of this company lies in the roadbed, and however exacting the specification, the reproduction cost of grading does [fol. 1352] not fully cover the element of value produced by time alone in the seasoning, weathering, and use. Even though it were possible to apply adequate unit prices to the various classes of material moved in the formation of a superior and stable roadbed, frequently all the quantities can not be inventoried. Often riprap or other roadbed protection is covered up by widening of embankments or rock and slag are placed in the emergency of washouts and hidden under the restored fills. Again, the natural disintegration of material on steep slopes loosens boulders and rock ledges which lodge within the roadbed prism whence they are removed at substantial expense with scarcely a trace of their ever having been handled. Mountain sides and canon walls are combed for quantities of boulders and unstable rocks without subsequent evidence of removal. The expense thereof is incurred for the betterment and safety of the roadbed.

In a newly constructed railroad natural slopes of repose are often disturbed and unweathered surfaces exposed in the excavation of cuts through material which on exposure disintegrates and slides or slips onto the track at lessening intervals as time goes on. Often the material of which embankments are made changes in character when exposed to the elements and slumps out of the normal roadbed prism

to form a stable footing for the restored slope and yet is not included in a reproduction inventory years later.

It is quite evident the cost of operation in transportation expense and in both maintenance of way and maintenance of equipment expenses over a newly constructed track and roadbed is higher than would normally prevail. The only [fol. 1353] rational basis that suggests itself for evaluating the betterment of the seasoning, weathering, and stabilizing process is in the excessive cost of operation for a period of years immediately following construction if such excess above normal can be approximated.

Q. Then, Mr. Ridgway, you would say it is difficult to evaluate with any degree of accuracy the value which does inhere in the old roadbed, would you?

A. Yes, it is impossible to precisely say.

Q. Do you say, then, that this nine million dollars, included in this exhibit, is the minimum amount which should be included for that purpose?

A. It is a matter of judgment, and I should say it is a minimum.

Q. Mr. Ridgway, you made this nine-million-dollar computation for presentation before the Interstate Commerce Commission at the time of its valuation of the properties of the Debtor, did you not?

A. Yes, sir.

Q. And testified in support of that contention at the hearing before the Interstate Commerce Commission?

A. Yes, sir.

Q. And the Debtor urged that point before the Commission, but the Commission refused to allow any additional value on that account?

A. That is so.

Q. Now, in the case of the D&RG, this additional value was obtained over a long period of years and had a much higher cost than you have estimated here, because of the fact that the D&RG was originally built as a narrow-gauge line; isn't that right?

A. Yes, that is partly the situation.

Q. Well, if it is not entirely correct, straighten it out. [fol. 1354] How would you express it?

A. I did not understand your question fully.

Q. Well, the D&RG was originally built as a narrow-gauge line, was it not?

A. Yes.

Q. And this additional value in its roadbed came about very slowly, did it not?

A. Yes.

Q. And at great expense because of the necessity of changing from a narrow-gauge to a standard-gauge railroad?

A. Well, the cost of the physical development, yes, to its present condition would be higher by reason of the various technical changes that have taken place in the 60 or 70 years.

Q. Was that change from narrow gauge to broad gauge made during operation? Explain that to me.

A. Oh, yes, most of it was. There was some of the property constructed standard gauge originally, but most of the property was constructed narrow gauge and then transformed or converted into standard gauge, 3-rail first, and then standard gauge subsequently.

Q. And because of the change in the way it was done, historically, would you say that the actual cost to the Debtor was in excess of the amount which you have here estimated for cost of development of the property?

A. Well, I judge it was, yes.

Mr. Goree: That is all. Is there any cross-examination of Mr. Ridgway?

(Witness excused.)

* * * * * * * *

[fol. 1355] IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO SITTING AT DENVER

No. 8669

In Proceedings for Reorganization of a Railroad

In the Matter of the DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, Debtor

Excerpts from Hearing of October 23 and 24, 1942

HEARING ON PETITION FOR PAYMENT OF INTEREST ON SECURITIES

Be It Remembered that on, to wit, the 23rd day of October, A. D. 1942, this cause came on for hearing before the Honorable J. Foster Symes, Judge of the District Court of the United States for the District of Colorado.

APPEARANCES:

Henry W. Anderson, Esq., of the firm of Hunton, Williams, Anderson, Gay & Moore, for the Insurance Group Committee.

Henry McAllister, Esq., for the Trustees of the debtor, The Denver and Rio Grande Western Railroad Company.

William V. Hodges, Esq., of the firm of Hodges, Vidal & Goree, for the debtors, The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company.

Erskine R. Myer, Esq., for H. Allyn Hicks, Esq., Trustee of the debtor The Denver and Salt Lake Western Railroad Company.

William R. Eaton, Esq., for the City Bank Farmers Trust Company, as Trustee.

[fol. 1356] Mason A. Lewis, Esq., of the firm of Lewis & Grant, for the Chase National Bank of the City of New York, as Trustee.

Robert G. Bosworth, Esq., of the firm of Pershing, Bosworth, Dick & Dawson, for the Guaranty Trust Company of New York, as Trustee.

William W. Grant, Esq., and Morrison Shafroth, Esq., of the firm of Grant, Shafroth & Toll, for the Insurance Group Committee.

Langdon H. Larwill, Esq., of the firm of Lindsey & Larwill, for the United States Trust Company of New York, as Trustee.

Miss Norma L. Comstock for the Central Hanover Bank and Trust Company, as Trustee.

Emmet McCaffery, Esq., and Frank P. Lynch, Jr., Esq., for the Reconstruction Finance Corporation.

* * * * * * *

[fol. 1357] WITNESS T. A. THOMPSON

Q. The petition in this case alleges in Paragraph 1 that approximately $30,000,000 has been expended upon this property during the period of trusteeship, chargeable to capital account. I asked you if you could prepare for me a statement showing separately the expenditures charged to capital account for the D. & R. G. itself, improvements on leased lines, and total, and then divide that total between equipment and roadway structure. Have you prepared such a statement?

A. I have.

Q. Will you proceed to present it, and I shall offer it in evidence?

(Thereupon a document was marked for identification October 23, 1942, Hearing, Exhibit 1.)

Q. Is that the correct statement?

A. That is the correct statement.

[fol. 1358] Q. Those figures are made up by you or under your direction, and they are to the best of your knowledge and belief correct?

A. Yes, sir, they are.

Q. In Section 2 of the petition there are certain allegations as to the earnings of the property for this year as compared to 1941. When I say "the property" I mean the D. & R. G. Railroad, and I asked you to prepare a statement showing the actual earnings brought down to net income for the year 1941, and the actual for 1942 as far as it was available, and estimate it for the balance of the period of 1942. Have you such a statement with you?

A. I have (handing counsel document).

Q. You hand me a statement entitled "Condensed Income Account," and I will ask if the figures therein were made up

by you or under your direction, and if they are true to the best of your knowledge and belief?

A. They were and are.

(Thereupon a document was marked for identification October 23, 1942, Hearing, Exhibit 2.)

Colonel Anderson: I will offer this in evidence as October 23 Hearing, Exhibit No. 2, if you please, and I will give the stenographer four copies.

Q. In the fourth paragraph of the petition there are certain allegations as to the cash position of the Trustees' estate, and I asked you if you would prepare for me a statement showing the present cash position as of the latest date available, the estimated cash position as of the close of business on December 31, 1942, as nearly as you could make it, and would state also the obligations concerning the [fol. 1359] trust estate which might have to be met within the reasonably near future. Have you prepared such a statement?

A. I have (handing document to counsel).

Q. You hand me a statement showing the cash position as stated, with a list of obligations aggregating $14,944,112. Is that a correct statement of the situation as I have outlined it?

A. It is.

(Thereupon a document was marked for identification October 23, 1942, Hearing, Exhibit 3.)

Q. Now, I notice, Mr. Thompson, that you have included in that statement of obligations the payment of conditional sales agreements of $2,282,106. Does that refer to the purchase of these conditional sales obligations which the Trustees have recently had up and under consideration?

A. That is the exact amount.

Q. Yes. I also notice that you include in these obligations the purchase of additional freight locomotives, $3,044,706, of 1,000 freight cars, $3,582,300, of 300 dump cars, $990,000. Are you in a position to state whether that equipment is now under order, or when the delivery thereof is contemplated, or shall I have to call the Trustees on that?

A. I think you will have to call the Trustees on that.

Q. Very well. The improvement work authorized, but not completed, I assume that your answer would probably be

the same as to that because it is more of an operating problem?

A. Substantially, yes.

Colonel Anderson: Then, if Your Honor please, I would [fol. 1358] ask leave to introduce in evidence the statement identified and explained by the witness, as October 23, 1942, Hearing, Exhibit No. 3, and am prepared to distribute the same with your leave.

Q. Mr. Thompson, some reference is made in the petition and the motion which I have filed this morning to the depreciation fund, or the amounts now charged to operating expenses on account of the depreciation of equipment and the possible application thereof to this payment of equipment obligations. I asked you, therefore, in that connection to prepare for me a summary and statement showing the present amount of equipment depreciation being charged by the company, and, if any charge be made for road and construction depreciation, to furnish me a statement of that. Have you prepared such a statement?

A. I have (handing document to counsel).

(Thereupon a document was marked for identification October 23, 1942, Hearing, Exhibit 4.)

Q. The statement which you have presented to me shows the items I have indicated, and you believe those are correct?

A. I do.

Colonel Anderson: I would like leave to introduce this statement in evidence as Exhibit No. 4.

Q. Mr. Thompson, this statement of equipment depreciation, of course, only includes the present depreciation on equipment now owned by the Rio Grande, and does not include any estimate of depreciation upon the equipment suggested as proposed to be purchased upon the preceding statement I introduced?

A. This includes no equipment except what we have on [fol. 1361] hand.

Q. To the end that we might have full information as to the available resources from which interest and other charges might be paid, both of the Denver and The Denver and Salt Lake Railway Company, the latter being involved

in the plan of reorganization, I asked you if you would, with the consent of the President of that company, prepare for me a statement showing the estimated income account of The Denver and Salt Lake Railway Company for the year 1942. Have you that statement?

A. I have (handing document to counsel).

(Thereupon a document was marked for identification October 23, 1942, Hearing, Exhibit 5.)

Q. You present me a statement showing the income account of The Denver and Salt Lake Railway Company for the year 1942 for eight months actual and four months estimated. Is that a statement, to the best of your knowledge and belief, which was prepared by the auditor of The Denver and Salt Lake Railway, but you believe it to be correct?

A. Believe it to be correct.

Colonel Anderson: May I present that in evidence as Exhibit No. 5?

The Court: Why do you introduce this, Colonel Anderson?

Colonel Anderson: Simply because——

The Court: Showing that there is $581,000 that may be available for the payment of interest. It may only become available in the event of consolidation.

[fol. 1362] Colonel Anderson: No, sir, that is available for payment of interest by The Denver and Salt Lake whether there is consolidation or not.

. . . . . .

[fol. 1363] WITNESS T. A. THOMPSON

Q. I notice you have cash working balance required $1,250,000. Is that the minimum cash balance you feel you should have on hand at any one time?

A. That is what it means.

Q. That doesn't mean that is all you need to have on hand any day of the year?

A. No, you have to make provision for large payments in addition to that. That is just a working fund.

Q. And at this time of the year, say December 31st, should you have on hand that sum, or should you have on hand a larger sum?

A. Depending on your obligations that are immediately or due in the near future, some of which are indicated in that list of requirements.

Q. Which are normally, the low months of your year, when your cash balance goes down?

A. The first of July is about as low a point as you hit.

By the Court:

Q. Well, January, February and March have been your lean months in earnings, haven't they?

A. Ordinarily, yes, but your normal requirements mature in March, April, May and June, and even in July your tax payments.

Q. Generally speaking, the first six months of the year are the lean months on this property?

A. That is correct.

[fol. 1364] By Mr. McCaffery:

Q. Now, one other question, Mr. Thompson. I don't want to get you mixed up in the question of what is the fair rental of the Dotsero Cut-off, or anything like that, but, taking the agreement which, as I recall, was entered into in 1932, under which the Rio Grande was to pay, among other things, an amount sufficient to enable The Denver and Salt Lake Western to pay a five per cent dividend, have you computed what the amount due under that agreement as of December 31, 1941, would be? Can you state that figure?

Colonel Anderson: I think it is very far afield of what we are talking about here today. We don't think the agreement has any bearing on the situation, and if you paid out everything earned here, if you take a third away, you would have more than the entire interest on all the bonds of The Denver and Rio Grande this year. So why confuse the situation with something which has nothing to do with it?

The Court: The objection is overruled. He may ask him.

A. Will you repeat your question again?

Q. Have you computed the amount which would be due as of December 31, 1941, on the basis of the 1932 agreement which I described a moment ago, and can you state what that figure is?

A. $1,171,039.75. That would be to December 31, 1941.

Q. And that figure would increase at the rate of five per cent on what figure each year?

A. On $3,631,000.00?

Mr. McCaffery: I believe that is all, Your Honor. I would like to have the privilege of recalling Mr. Thompson [fol. 1365] later if it becomes necessary.

By the Court:

Q. Mr. Thompson, will you refer to this Exhibit 3, and if all the moneys are paid out there that are listed, beginning with the expenditures authorized and contemplated, you would show a deficit, would you not, on December 31, 1942?

A. Very certainly of approximately five and a half million dollars.

Q. In other words, you can't pay out all those items that are listed there and have any cash left the first of the year, can you?

A. That is right. Of course, Your Honor, most of those are not due to be paid as of December 31st.

Q. I understand, but if those payments were anticipated and made, you couldn't meet them?

A. That is right.

The Court: All right. That is all. Thank you.

Q. And the cash working balance required cannot be counted as available cash?

A. We wouldn't think it would be counted as available cash, because you do need a working fund.

Q. Necessary for payrolls and operating expenses?

A. That is right.

The Court: That is all.

By Mr. Hodges:

Q. Do you on your accounts accrue a rental of the Grand Junction line?

A. Yes, sir.

Q. Can you turn to a figure to show what the accrued rental on the Grand Junction line is now accrued and unpaid?

A. I can give you as of December 31, 1941.

[fol. 1366] Q. That is close enough.

A. $658,333.33.

Q. What is the annual accrual?
A. $100,000.00.

By Mr. Bosworth:

Q. $100,000.00?
A. $100,000.00.

By the Court:

Q. $100,000.00 a year?
A. Yes, sir.
Q. If that money was paid to them they would have to apply it on interest on their bonds?
A. Yes, sir.
Q. And that would relieve the Trustees of paying that interest otherwise?
A. The Rio Grande Junction is charged as rental theoretically, used by them to pay interest on its bonds.
Q. Instead of that, you say you have paid it in direct taxes?
A. That is correct. We happen to be auditor of both companies.

By Mr. McCaffery:

Q. Who owns the stock of the Rio Grande Junction?
A. The Rio Grande Western Railroad.
Q. All of it?
A. Subject to the lien of the Refunding and Improvement Mortgage.

By Mr. Myer:

Q. Mr. Thompson, can you accrue the obligations of The Denver and Salt Lake Western and The Denver and Rio Grande on the note of $3,110,850.00, known as the stock purchase loan?
A. No, of December 31, 1941, offhand I can't answer your question.
Q. Will you furnish me a statement of that?
A. I will have to look at the balance sheets.

Colonel Anderson: When you say "the stock purchase [fol. 1367] loan," do you mean the purchase of the Denver and Salt Lake stock?
Mr. Myer: Yes, sir.

By Mr. Hodges:

Q. The rentals under the lease of The Denver and Salt Lake road are paid, aren't they?

A. They are being paid currently.

Redirect examination.

By Colonel Anderson:

Q. Let me ask you, you have Exhibit 3, haven't you, that statement? You have been asked a number of questions about the obligations set up in Exhibit 3. I will ask the cash statement in the first two lines, as I understand it, is your actual cash to date and your estimated cash balance on December 31, 1942?

A. That is right.

Q. That is as stated. Now, as I understand it, you are not prepared to say when, if at all, the obligations for conditional sales agreements of purchases of Diesel freight locomotives or the 1,000 freight cars or the 300 dump cars will become due?

A. No, sir, I am not.

Q. With the possible exception of a few of the cars they are certain not to become due until some time in 1943, are they?

A. That is my information.

Q. Yes. Now, as to work authorized and not completed, you are not in a position to say when that will be done and when it will be payable?

A. No, sir.

Q. If it was not completed until 1943, or because of difficulty of priorities or other reasons was not completed at all, then that would affect the statement to that extent, [fol. 1368] would that not be true?

A. That is correct.

Mr. McCaffery: Why doesn't Colonel Anderson ask Mr. Swan the questions that Mr. Thompson is not capable to answer?

Colonel Anderson: Mr. Thompson was asked to answer these things.

Q. Now, the ad valorem taxes are not due until 1943, are they?

A. This, as I believe I have in the record now, covers only the first half of the Colorado taxes for 1942 which are payable on February 28th, and the last half of the 1942 for New Mexico which are payable on April 30th.

Q. April 30th?

A. That is right.

By the Court:

Q. Next year?

A. Next year.

By Colonel Anderson:

Q. Now, Federal and State income taxes, that they may accrue, certainly as to Federal are not payable until March 15th of next year?

A. March 15th of next year.

Q. So that you are giving the cash balance as of October 21st, and you are only giving those things which may accrue as of December 31st and next year to the extent they are paid?

A. To the extent that I consider them commitments against this year's earnings.

Q. But if they do not become due this year they are not payable in this year?

A. That is a debatable question. I wouldn't attempt to answer it.

Recross-examination.

By Mr. McCaffery:

Q. Do you know as to these Colorado taxes Colonel Ander- [fol 1369] son was asking about, when they become an obligation as distinguished from when they become payable?

A. Theoretically they are due on January 1, 1943, for 1942. That is the date of your tax bill, and they are then due.

Q. Is that true of the New Mexico taxes as well, do you know?

A. I am not certain about New Mexico.

The Court: That is all. We will excuse you, Mr. Thompson.

Colonel Anderson: I will offer Mr. Swan.

(Thereupon a recess of five minutes was taken.)

HENRY SWAN, being called and sworn as a witness on behalf of the petitioner, the Insurance Group Committee, testified as follows:

Direct examination.

By Colonel Anderson:

Q. Mr. Swan, you are one of the Trustees of The Denver and Rio Grande Western Railroad, aren't you, in this proceeding?

A. Yes, sir.

Q. Mr. Thompson, the General Auditor, has introduced while on the stand an exhibit showing your present cash position, the estimated cash balance.

The Court: Would you mind referring to the exhibit?

Colonel Anderson: Statement Exhibit 3.

The Court: October 23rd.

Q. Introduced a statement, October 23rd, showing your actual cash, and your contemplated cash position or estimated cash position as of December 31, 1942. He has then listed certain obligations in that statement, and it is about these that I would like to ask you. Have you a copy of that [fol. 1370] statement before you?

A. Yes, sir.

Q. Now, take the payment of the conditional sales agreements. As I understand, he testified that those are made up with your cooperation. That refers to the conditional sales agreements for equipment, anticipation of which you have had under contemplation, have you not?

A. Yes, sir.

Q. Those obligations, aggregating in round numbers $2,282,000.00, are not due at this time, are they?

A. They are payable in monthly installments.

Q. Over a period of years?

A. Yes, sir.

Q. Have you before you the amount of the monthly installments applicable to the several items making up that amount?

A. No, sir.

Q. Take them in their order. One is Electro-Motive Corporation $62,056.80, as I understand. Do you know when that is due and payable by its terms? I mean the last installment.

A. It tells right on the statement.

Q. Let's see.

A. That covers the Diesel switching locomotive for use at Remco. It was financed originally by General Motors Acceptance Corporation with the higher coupon that we were successful in transferring to a bank to handle at a lesser rate to maturity, payable monthly with interest.

Q. And you don't know now the amount of the monthly installments?

A. No, sir.

Q. You don't know when the last one is due?

A. I don't recall.

Q. But the last one will not be due——

A. Not due for several years.

Q. Not due for several years?

A. No, sir.

[fol. 1371] Q. Those installments run over a period of several years?

A. Yes, sir.

Q. That is sufficient. Now, take the Northern Trust Company, thirteen Diesel locomotives, $545,318.00. I assume you are not able to state the actual amount of the monthly installments?

A. I can't give you the monthly installments, but it is my recollection that it was placed a year last June.

Mr. McCaffery: You say "take the Northern Trust Company." There isn't anything about the Northern Trust Company in this exhibit, is there?

Colonel Anderson: No, but I have a list of them. They are included in that list.

The Witness: That covers fourteen Diesel switching locomotives that we purchased a year ago last summer or spring.

Q. And that is a part of the $2,282,000.00, round numbers, mentioned on the statement, Exhibit No. 3?

A. Correct.

Q. And that was originally placed in about June, 1941, payable in equal monthly installments over a period of ninety-one or ninety-six months?

A. It was ninety-six months.

Q. Ninety-six months?

A. Yes, sir.

Q. That would be eight years?

A. That is correct.

Q. And only a little over one year has passed; isn't that right?

A. That is correct.

Q. Now, take the next item that you furnished me as making up that, the Baldwin Locomotive Works for five steam locomotives.

A. That is $710,369.91.

Q. Can you give me the information about that substan-
[fol. 1372] tially as you have given it?

A. That was placed at about November of 1941, and was one to seventy-two months, six years.

Q. Provided equal monthly installments of payment over a period of seventy-two months?

A. Yes.

Q. That has run about one year?

A. A little less than a year.

Q. A little less than a year, and it has a little over five years additional to run on that basis?

A. Yes, sir.

Q. Now, the Electro-Motive Corporation, three Diesel freight locomotives, $964,361.00 makes up the remainder of the amount as furnished to me by you. Could you give me the same information about that obligation?

A. That was placed, I think, last February, and was on a one to seventy-two month basis, payable monthly, interest and principal.

Q. And therefore it has run about eight months?

A. That is right.

Q. Eight installments have been paid, and the remaining of seventy-two installments, that is, sixty-four installments, probably a period of a little over five years, are yet to be paid?

A. If we pay for December we will have ten installments made, and we will have then the five years and two months until the last installment is paid.

Q. Before these installments all mature?

A. Yes, sir.

Q. Now, taking up the purchase of Diesel freight locomotives, taking up the next item on this Exhibit 3, the purchase of Diesel freight locomotives, $3,044,706.00, would your tell me the status of that item as to the contract when possible delivery is expected, or whether you have any definite

[fol. 1373] information as to delivery, etc., any information you can give in regard to it?

A. We received the court order a number of months ago for the purchase of these locomotives. We placed the order with the Electro-Motive Corporation, and were promised delivery commencing September 1st and having one locomotive delivered each five days thereafter.

Q. That was a promised delivery September 1st this year?

A. Yes. In the last of July we were advised that it would be impossible for them to complete the delivery as scheduled, and they have been deferred until probably some time in the first quarter, possibly late in the first quarter, of 1943, and we are hopeful of getting them at that time.

Q. But you can't say more than that you are hopeful in view of the present condition of government control over that kind of manufacture?

A. That is correct.

Q. You can give no definite assurance as to the time of delivery, nor can they give you definite assurance?

A. That is correct.

Q. As a matter of fact, the Electro-Motive Corporation is subject to government control?

A. That is correct.

Mr. McCaffery: I think the witness instead of Colonel Anderson should testify.

The Court: I think that is correct. Let him testify instead of you.

Colonel Anderson: I wouldn't undertake to lead this witness for anything in the world. (Laughter.)

Q. Now, there is nothing payable on account of those locomotives until they are delivered?

A. No, sir.

[fol. 1374] Q. That is right?

A. Yes, sir.

Q. Now, take the 1,000 freight cars, could you give me similar information as to that, it being the next item on Exhibit 3? Any information you can give?

A. We have received court order for the purchase of these cars. We have placed our order for the construction of them with the Pressed Steel Car Company, and we have received the proper clearance from Washington for the delivery of 780 of these cars in the last quarter of this year, and 220 in the first quarter of next year.

Q. And if deliveries are made as in accordance with those assurances, the payments will have to be made at those times for the numbers you indicated?

A. As delivered.

Q. As delivered. That is the way they are payable. Have you made any arrangements for financing these obligations, that is, the obligations as to the Diesel freight locomotives and as to the freight cars, by equipment trust or any other manner at this time?

A. No, sir, we contemplate paying for them from our cash resources.

Q. You have had a good deal of experience in financing these things on equipment trusts, haven't you?

A. It is timed with the years we have been on the property.

Q. That is what I thought. You don't think there would be any trouble of financing on equipment trusts?

A. With conditions as they are at present there will be no difficulty, and in any event the Reconstruction Finance Corporation has indicated its willingness to take care of the requirements for payment on this additional equipment.

By the Court:

Q. Weren't you ordered or requested to buy these by the [fol. 1375] government for the government plants on your line?

A. There are numerous of the government plants on our line, but the two particular plants which occasioned primarily the acquisition of this particular equipment are the two steel plants, one located down near San Bernardino, California, and the other one located at Geneva south of Salt Lake and north of Provo on our line. We were advised that we were expected to be able to furnish the power and the cars to haul the coal that was to be necessary, or coke, some of the finished product, and very recently we were told that we were to handle the lime rock and dolomite for the Geneva plant from our Tintic branch. That is what occasioned the inclusion of the 300 dump cars, which is the next item. When originally contemplated, it was proposed that the Union Pacific would haul the iron ore and the lime rock or the dolomite. Just recently we have been advised that the Union Pacific was not expected to do that, but that we were, and we have already made the appropriate arrangements for the placing of the rail and sidings to acquire

the facilities that are necessary to run the lime rock and dolomite for transmission to the plant at Geneva. In addition to those which we are purchasing here, the Defense Plant Corporation, which is a subsidiary of the RFC, is furnishing to us on a rental basis, paid for by the Defense Plant Corporation, and not by the trusteeship, six steam freight locomotives. Those were originally ordered by us on behalf of the Defense Plant Corporation because of the priority position which we occupy by reason of having given the Baldwin company an order prior to this arrange-
[fol. 1376] ment. More recently, however, the WPB has ordered the locomotives constructed there by the American Locomotive Company, not from our specification, but from the specification of the Union Pacific Railroad. In addition to these locomotives, the Defense Plant Corporation will furnish to us at a rental basis 500 gondolas, flat bottom gondolas. It is our intention to come into this court shortly for authority to purchase 300 dump cars, and we hope to have them included with the 220 that will be delivered to us in the first quarter of next year under the railroad pool.

Q. Under what?

A. The ones that are allotted to the railroads for construction, so many a year.

Q. When you refer to 300 dump cars, you refer to the next item on the exhibit, I think, of $990,000?

A. That is correct.

Q. There has been no court authority for the purchase of those yet?

A. No, sir.

Q. And no obligation is figured with respect to that as yet, is there?

A. No, sir.

Q. They are something that you are going to ask court authority to buy in the future?

A. Very shortly.

Q. Yes, well, very shortly, then. Now, the improvement work authorized, but not completed, is an item in this same exhibit of $3,100,000. Could you tell me something about the status of that and the prospect of its completion, and your requirements on account of paying for that work, how they run?

A. We tentatively, in estimating our financial needs for next year, have contemplated that we would do two and a quarter millions of work on lines from an improvement
[fol. 1377] program standpoint in the first six months of

next year. That means that if we could devote that entire work solely to the completion of this work authorized, but not completed, there would only be a little less than $900,000 of the carry-over items yet to do.

Q. You mention $900,000 worth of work now authorized, but not completed.

A. In addition there will be a new improvement program which will be presented to this Court after the present peak of business is over, which we will ask for authority to do next year.

Q. That is in the year 1943?

A. That is correct. So we will probably do a part of that new work plus a part of the carry-over work in that item of two million and a quarter which I have indicated will be expended in the first six months of next year.

Q. You mean all this nine hundred and odd thousand dollars is a part of uncompleted—as a part of your authorized program for 1942 may be carried over into the 1943 year program?

A. No, I don't make it clear. In our estimate for the first six months of next year cash requirements we contemplate that we will be able to do two and a quarter million dollars of improvement work on line.

Q. During that six months?

A. During the first six months of next year. What I meant to convey was that all of that work on line work that consists solely of items in this carry-over, we would complete all but about $900,000 of the carry-over, but we will not do merely work on the carry-over. We will do some work we will present to the Court de novo. Therefore we contemplate doing only two and a quarter millions of the [fol. 1378] work on the carry-over and the newly authorized items in the first six months of 1943.

Q. Now, in order to make it comparable to the cash statement above, have you any idea of how much of that improvement work you contemplate that will be completed, and therefore have to be paid for in the remainder of this year—two months of this year?

A. I understand that this $3,100,000 is as of December 31st, but you could ask Mr. Thompson. I didn't prepare that figure.

Q. No. I understood him to say it was not. We asked him, and he said——

A. From this date on.

Q. Yes, from this date your improvement program, looking forward.

A. Well, I don't know how he arrived at the figure, because I didn't prepare it, but I do know that we will have over $3,000,000, or at least I think I know, for next year of the carry-over.

Q. In the first six months of next year. All I wanted to gather was, Mr. Swan, if you had information as to approximately how much you would have to pay for between now and until December 31st.

A. Well, Colonel, I understand in preparing this $9,557,000 estimated cash balance, it was that cash balance which remained after doing improvement work from this date until December 31st.

Q. I see. Everything in the way of improvement work will have been paid for?

A. In this year.

Q. That is what I am getting at. So this item of $3,100,000 is not anything you have to pay this year, but will be paid in a period of six months of next, provided the authorization is given by the Court which you have suggested you are going to ask?

A. Well, that is carryover. The new budget has not been [fol. 1379] presented.

Q. But all the payments you have made up to date have been already deducted in arriving at the $9,557,000.00 to December 31st?

A. That is our estimate.

Q. I mean up to December 31st all payments are deducted before arrival of that?

A. Except these items which are listed below for future delivery. Part of them might be this current year.

Q. But, as far as you know, the charges against your cash for the current year for improvements are taken care of before you arrive at the $9,557,000?

A. Yes, sir.

. . . . . .

[fol. 1380] Q. Would it be a fair statement, Mr. Swan, that as a result of the present traffic running over the road, the road is being worn out in actual operation faster than the normal rate?

A. It would be very difficult to answer that question except to this extent. It is perfectly obvious if you run 2,000,000 ton miles over a section of road instead of 1,000,000

in the same period, or have twice as much wear on the head of the rail.

Q. Are you familiar, Mr. Swan, with the recent regulations of the Interstate Commerce Commission which contemplate the possibility of setting up a reserve now for depreciation which cannot be taken care of now because of priorities or some other reason—setting up that reserve for taking care of the depreciation later?

A. I have heard it, and that is now in the hands of Mr. Thompson and Mr. Hart of Mr. McAllister's office for consideration and application in our own case.

Q. You have not set up such a reserve; and this $700,000,00 doesn't include any amount in respect of a reserve of that character?

A. No, sir.

Mr. McCaffery: I think that is all.

By Mr. Myer:

Q. Mr. Swan, in Exhibit No. 3 is your estimated cash balance of December 31, 1942, at $9,357,000,00—does that take into account any rental on The Denver and Salt Lake Western Railroad?

A. No, sir.

Q. Does it take into account any rental on The Denver and Salt Lake Railway Company line?

[fol. 1381] A. It is after payment of any rentals that may be due the Denver and Salt Lake.

. . . . . .

[fol. 1382] A. The impact of the petition that is under consideration today on the fiscal problem of the Trustees is of such a serious character that it seems to the Trustees that they should present to this Court the methods which have been adopted in their endeavor to conserve the financial integrity of the property while it is being operated by the Court, especially so as some very serious problems present themselves to the Trustees in connection with the plan which has been proposed by the Interstate Commerce Commission. The average age of the equipment on this railroad is as follows: on standard gauge locomotives it is 26.19 years old. Please bear that figure in mind, 26.19 years. The standard gauge freight cars have an average age of 22.27 years. The standard gauge passenger cars have an average age of 23.79 years. The high maintenance of equip-

ment ratio reflected in our operating statements is due in very large measure to the high average age of this equipment. The high operating ratio has been due in large measure to the high average age of this equipment. At the present time we are being forced by circumstances to contract for and acquire equipment to handle this accelerated load, and thereby we incur heavier obligations for subsequent liquidation than had been contemplated. In making an approach to the equipment problem we had a study made, not of the locomotives or of the passenger equipment, but of the standard gauge freight equipment by classes. This was done a number of years ago, in 1938 if I remember correctly. And this was done after a physical inspection of over thirty per cent of the units in every class. And we [fol. 1383] then determined to chart what we were pleased to term the economic utility of the equipment surveyed, and determine whether or not certain repairs could be given to that equipment, and keep it in life and use it for certain longer life as against an immediate purchase of new equipment. Those charts developed some rather interesting thoughts. If we were to undertake to replace the equipment too rapidly, we would not have enough available cash in the depreciation fund to take care of the down payment on the new equipment if financed either by conditional sales contracts or equipment trusts, to take care of the serial repayments upon those outstanding equipment trusts or conditional sales contracts that we contracted earlier, or had been contracted by the debtor corporation, to pay interest, and to pay the cost of repair or improvement, and I prefer to use the word "improvement" rather than the word "repair," to existing equipment on line, not only the operating expenses incident to improvement, but the capital charges resulting from such improvement. I am going to illustrate a little later on the blackboard some of this problem so you can see it more clearly, but if we put side frames on cars under Interstate Commerce Commission order, in order to effect interchange, a certain amount of that work becomes capitalized, and a certain amount perhaps would be charged to operating expenses incident to improvement. I am going to present you a chart and some statistics which have been prepared, but for the moment I think it appropriate to state that during the period of the trusteeship the operating expenses incident to improvement and the capitalized value of the improvement have averaged

[fol. 1384] $596,000 each year. Of this $596,000 about $135,000 has been operating expense and charged out of the earnings. Four hundred and sixty odd thousand dollars have been capitalized. The reason I expose that condition to you is because the problem of acquiring the money over and above the depreciation fund is one that must be cared for in some manner other than from the depreciation fund. Now, in addition to those thoughts, it had occurred to the Trustees that it was their duty to provide the interest earned under a plan proposed by the Interstate Commerce Commission, to be available when that plan should become effective, and that is one of the problems that the Trustees have kept in mind continuously. It did not occur to the Trustees, however, that it was necessary to earmark dollars, or set them off into a trust fund, provided they kept the facilities which would enable the moneys to be raised when and as they were needed on clear equipment which the Trustees might have. However, when this thought was expressed to Colonel Anderson yesterday, he presented the Trustees with a thought that they had not considered, and that was this: Does the property of the trusteeship and especially the equipment property belonging to the Trustees have a lien against it under an after acquired property clause of one or more of the defaulted bond issues of the debtor corporation? We had not considered that. There is another factor too that had been brought up at that discussion with Colonel Anderson. That was that the Interstate Commerce Commission might not look with favor upon any railroad while it was still in private ownership or the hands of the Court, approaching it for authority to issue either equipment trust certificates or the confirmation [fol. 1385] of loans in some form, if an adequate cash balance was in the hands of the railroad. Now, practically that means this, in so far as the Trustees have interpreted it. If we had good sources of credit, our cash balance could drop quite materially as against some future day when a heavy cash demand would be made on the Trustees, at which time they would avail themselves of this credit. Now, it was because of our belief that our credit was good and that we could avail ourselves of banking facilities, that we felt it to the best interest of the trusteeship in the first instance to save interest. In the second instance it was deemed desirable from the standpoint of the solvent reorganization to get behind the trusteeship as rapidly as possible all of the costs of the new equipment, not by borrowing money,

but by paying cash for the new equipment out of the swollen earnings resulting from the use of the new equipment, because of the terrific impact upon the operating statement of the railroad's future requirements, and especially in the primary post-war depression. I will illustrate that thing in this manner. Would you like to offer an exhibit, Mr. McAllister?

Q. Yes.

A. These exhibits are being offered in the interest of a clarification perhaps of the fiscal policy of the trusteeship, and you can put that in any form you want, and pass them around. Now, have you all got copies of the blueprint and the sheet? I will refer to the sheet, and we will put the blueprint aside for the moment. Refer to Exhibit 8. This is a statement of the average earnings for the years 1930 to 1941, inclusive.

[fol. 1386] By the Court:

Q. Exhibit 8?

A. Exhibit 8. That is the little sheet. You have the blueprint in your hand.

Mr. Shafroth: You have Exhibit 7. The little sheet is marked Exhibit 8.

The Witness: If you will look down you will see "Available for Interest on Funded Debt $2,362,933." Please keep that figure of $2,362,933 in mind. When you deduct roadway depreciation you take off about $700,000, and it reduces to $1,633,074. Now, bearing in mind that figure of $2,300,000, and turning now to Exhibit 7, not the blueprint, but the printed sheet which is labeled "Present and Projected D. & R. G. W. Annual Equipment Disbursements Compared with Annual Depreciation Accruals," in column 1 you will find payments on present obligations, principal and interest. In the second column you will find the depreciation charge. Now, while we are on the question of depreciation charge it might be well to point out that the Trustees have had the feeling, which I think is probably current with other railroads, that the depreciation account should take care of those items which I mentioned a while ago, namely, down payment on equipment, serial payments on outstanding equipment obligations, interest, and improvements to existing equipment. You will observe that just this current year we are $1,000,000 short in our depreciation charge of covering the situation. Now, under

some recent rulings railroads that have paid to acquire equipment to prosecute the war effort are permitted to make an amortization charge. This becomes a charge against operations, and while the funds may be earmarked, [fol. 1387] some lawyer will have to interpret the use to which they can be put and still keep within the law. I don't know enough about it, but it is obvious that if you had $2,300,000 or practically $2,968,000 you are over twice this current year's depreciation charge. Now, in addition to that, if we add the $596,000 less the $135,000 incident to improvement, or $461,000 to that sum, you have over $3,300,000 as against the depreciation charge of $1,380,000, and if you deduct $1,380,000 from the $3,300,000, that resulting in $2,060,000 net result, demand for cash if you will, you have more than enough demand for cash than you have average earnings less roadway depreciation available for the ten years or eleven years preceding this year, and you could not put through the plan proposed by the Interstate Commerce Commission. Now, then, how are we going to finance these items which we have discussed today, the cars, the Diesels? It was our purpose to utilize the available cash balance this year only to pay off the outstanding conditional sales contracts which were kept optional for this specific purpose, and it was our expectation on behalf of the solvency of the reorganized property to utilize the windfall of earnings, and thereby the cash that comes from it, for eliminating any charges to the depreciation fund from the date of purchase of the new equipment by paying for them in cash. If that be done, the figures shown on this computation will be quite different. There will not be so heavy payments on present obligations or on future obligations. The depreciation charge will not change very much in spite of the fact we are acquiring new equipment, because the old equipment is so old that it loses its depreciation value about as fast or [fol. 1388] faster than the new equipment creates additional value. So if you will observe, in the third from the last column we have made no depreciation charge because of that offset. Now, in the last grand total you will find that amortization and depreciation offset against the disbursements for the next couple of years lags behind the disbursements. After that it catches up for a bit. But if that is the period during which the reorganization becomes effective, unless the earnings step up, the lag will probably make it impossible to earn the fixed charges set up in

the plan. If anybody would like to have me do so I will illustrate this process on the blackboard. It is all set up here if I have gone too fast for you. It is easy for us to follow it because we follow the outlines in it. If you want, I will work it out on the blackboard. We would like to have the Court consider, in view of these statements and the effect and impact it will have upon the reorganization unless we are going into a protracted war period where earnings will be comparable to this year—to have the Court determine whether it is wise for us to pay off these conditional sales agreements, or whether the Court would prefer to have us leave them outstanding. The Trustees would also like to have an expression of opinion, advice and guidance as to whether they should borrow against the new equipment, or conserve the cash as much as possible to pay cash for the new equipment. It is our best expectation, or it was our best expectation prior to the presentation of this petition today, that they would be able, out of the profits and earnings of this railroad, out of the amortization fund and the depreciation fund, to pay cash for all of [fol. 1389] the equipment that is listed and presented here today, and still have on July 1st next and prior to the heavy fall business where we receive the greatest amount of our gross income, very substantial cash balance sufficient in the aggregate to care for this plan if it shall be declared effective by that time, sufficient to care for our income taxes contemplated, to care for contingencies that might arise, and be in a solvent position.

The Court: Does that conclude your statement?

The Witness: That is all unless someone wants to ask questions, or you want me to explain some of these figures.

Mr. Hodges: I would like to ask a question.

By Mr. Hodges:

Q. I will ask Mr. Swan if in his studies he has taken into consideration the problem of the income tax based on the gross operation of the property.

A. We have. This matter has been receiving study for some months by Mr. McAllister and his associate, Mr. Hart, and by our Chief Auditor, and these studies indicate we shall have very substantial payments to make, with resultant shock to our cash position, but the complete extent of this problem has not yet been finally determined.

We are prepared to take care of such contingencies as may arise in accordance with our previous approach to this problem. If we shall pay interest as petitioned and should pay off those conditional sales contracts it might embarrass us some.

Q. It sums up that you have not in these estimates that you have made taken into consideration any tax payments that may have to be made?

A. Oh, yes, in Exhibit 3 of Mr. Thompson's this morning we put in $1,300,000 federal and state income taxes. If that should not be enough we still have considered it in [fol. 1390] the matter of contingencies.

Redirect examination.

By Colonel Anderson:

Q. Mr. Swan, I would like to offer just a very few questions for clearing up some of the points which I obviously did not catch. It is very hard to make notes as you go along. You spoke of the fact that depreciation on equipment was not adequate for the year 1942 to meet your installments on equipment as shown by Exhibit 8 by about $1,000,000, and for the year 1943 your depreciation exceeds your obligations, and during that year both principal and interest by a few thousand dollars. Now, is it not a fact that your maturities of principal on most of this equipment which has been purchased runs only a period of ten to fifteen years, while the life of your equipment and the period in which it would bear depreciation runs twenty-five to thirty years, taking it as a whole?

A. That is correct, Colonel.

Q. In other words, if you were to pay off your equipment maturities on locomotives, we will say, in a period of ten years, the depreciation on those locomotives might not provide all the money necessary in that ten years to pay the amortization charges which would relieve them from any other debt, but after that debt was paid partly from depreciation and partly from the earnings, the equipment would continue to provide a depreciation fund which would go into cash to reimburse the company for the amount it had to advance to pay off those short-term installments?

A. There will be a time when the obligations will taper off, but the depreciation fund continues. I might add to

[fol. 1391] that; but that does not include the demand for the cash in the immediate future for the amortization fund and for the improvement to existing equipment.

Q. Well, your improvement to existing equipment is charged to capital, but, of course, has to be paid out of cash, and if you have accumulated a considerable amount of equipment which is free from obligation, the depreciation on that accumulated equipment could take care of the necessary money for this improvement, and is carried in the cash through operating expenses whether you use it or not; isn't that true?

A. Not in accordance with this exhibit. If I read this exhibit correctly, Colonel, we only have a depreciation, etc. of two million two hundred and fifteen thousand odd dollars, but we have disbursements this year of $3,687,000. Next year we will have an amortization and depreciation, in the last column, of three million four hundred odd thousand, and we have calls on us for $3,661,000. Now, then, I am perfectly willing to admit that on the eighth year we will have an accumulation of cash which, if you want to borrow again against your equipment in anticipation of your depreciation fund working out, it might be one method of reaching it. That is one of the things I have had in mind in trying to handle this big load. We would not think of buying this equipment under our equipment budget at this time. Our problem is: What will the Trustees do to make possible an earning capacity to justify the Interstate Commerce Commission plan? This is a fact. This is no theory.

Q. Well, Mr. Swan, I didn't mean to get into an argument of that, because the proper place for me to argue that is before the Court. All I wanted to do was to make [fol. 1392] it perfectly clear what you mean about this depreciation, and to bring out the fact that the variations which you pointed out here in available funds from depreciation, and the demands in the way of interest and amortization, were brought about by the fact that the installments of amortization did not run for the life of the equipment, and they necessarily varied on that account. In the earlier period it might be more than the available depreciation. In the later period it might be very much less than the available depreciation. That is all I wanted to bring out in that connection, and you have answered my question. Now, I didn't quite catch what you said when

you referred to my statement made on yesterday, which I didn't think you got entirely as I intended for you to get it, and I will therefore just ask you to clear up in my mind what you did say.

A. I am glad you do, Colonel, because it is a legal point and I am no lawyer. I think I mentioned yesterday in our conversation that it was in the minds of the Trustees that if the cash balance became low later, they would have free equipment on which they could again borrow if they paid off these conditional sales contracts. I think you said there was some difficulty in getting an adequate and appropriate and legal and satisfactory equipment trust from company owned equipment by reason of the after acquired property clauses on mortgages, and because of the method of ownership, and then you emphasized again the possibility that the equipment was not free anyway in the hands of the Trustees because of the after acquired property clauses in some of the mortgages of the debtor corporation. That is the impression that I got.

[fol. 1393] Q. Well, I wanted to say that I think you somewhat misunderstood me, and I want to clear it up that I did not refer specifically to that after acquired property clause, but I did say that I was inclined very strongly to the view, without expressing an opinion to you when you have a very able lawyer, that that equipment would be subject to the mortgages, any and all of these mortgages, because the use of the funds which would be allocable on the respective mortgages would give them the right to levy on the basis they contributed to this fund. I did not state the legal position.

Mr. Shafroth: That is absolutely correct. The Colonel did not mention anything about the after acquired clause.

Colonel Anderson: I was careful to avoid the legal proposition because I am not tying myself down on that, and I want to argue it.

Q. On the second question you spoke of my views of the I. C. C. position. Of course, I don't want to be put in the position of stating the position of the Interstate Commerce Commission any more than I would in stating the position of this Court in anticipation, but I do know that they have had some very serious experiences in railroads in lending on second-hand equipment, that is, equipment

which has been purchased, and the question of whether or not they could do that.

The Court: Are you testifying now, Colonel?

Colonel Anderson: No, sir, but I didn't want my statement—I am sure Mr. Swan didn't want my statement on the record quite different from what I made to him.

The Witness: No, I do not.

[fol. 1394] Q. And I think you will admit I stated that?

A. Well, you gave me a great shock when you showed me those two statements.

Q. Well, I don't want to impute to the Commission that statement as to what they would or would not do. Now, may I ask you this question: If you feel that there is a probability or a reasonable possibility that you may have to borrow money upon equipment upon which you have paid these additional sales agreements or liens, may I not suggest that it might be better, or would it be your view to let these obligations stay out, and keep your cash position, rather than paying them off and borrowing money again for the purchase of new equipment?

A. If it seems desirable to keep strong in cash or pay it out in interest, it would seem undesirable to pay off the conditional sales contracts, and then have to go back into the market sixty or ninety days thereafter and borrow on some of the newly purchased equipment. I tried to present in this thesis the apporach of the Trustees to the whole problem on a long range planning basis than for the payment of interest, which more or less erupted in our face when we were in the midst of the program.

Colonel Anderson: That is all, Mr. Swan. I may want to clear up those points.

Mr. Hodges: I would like to ask a couple of questions.

By Mr. Hodges:

Q. Mr. Swan, much of your showing there is projected on the average performance of 1930 to 1941, inclusive, is it not?

A. It is projected against 1930 to 1941 average because [fol. 1395] that was the period that apparently was taken by the Interstate Commerce Commission in the fixation of fixed charges under the new plan. And what I was trying to develop, Mr. Hodges, was what the impact of

the large use of the depreciation fund, plus the amortization fund, plus the use of funds, cash possibly, for the improvement of the existing equipment, would have on that plan, especially after you deduct the original depreciation.

Q. And if there was error in the assumption that that period fairly represents the performance of the property that may be expected in the future, either imminent or remote, it does affect the validity of your conclusions, does it not?

A. If the road shall do as well after this war period has passed as the average of 1930 to 1941 it is obvious that there will be money available for the fixed charges. If the road continues to do as well as it does in 1942, the problem does not need to concern us.

Q. Now, may I ask you another question. I notice you set up a tentative figure of approximately $700,000 a year for depreciation and road construction, and I believe you did explain that that was tentative for the moment—represented no permanent policy. What does the setting up of that depreciation have to do with your accounting of maintenance expenditures; anything?

A. The maintenance expenditures, as I understand it—I prefer you ask Mr. Thompson because he is more familiar with the Interstate Commerce Commission rulings than I am, but that maintenance is one thing, and your depreciation is another thing, and can be used primarily for capital reinvestment rather than as against current maintenance. [fol. 1396] We have the same thing on the equipment. You have a depreciation fund, but you also have maintenance of equipment. The depreciation fund comes out of your operating expense, and, as a matter of fact, it comes into the cash drawer and is paid out. In the operation of this particular railroad I think the depreciation fund was used to buy Moffat Road stock. I don't think they earmarked the dollars.

Q. I don't want to go too deeply into this question of depreciation, but you do know that over the years the railroads have resisted the setting up of road and structure depreciation as is now suggested. You are familiar with that?

A. Yes.

Q. And they did acquiesce in the setting up of an equipment depreciation?

A. That is right.

Q. And that there was in their estimation a difference in principle involved, and that they considered that the maintenance well maintained precluded inspection depreciation, and therefore resisted that setting up of that figure; are you familiar with that?

A. I am familiar with that, Mr. Hodges.

Q. But in setting up this figure you make no difference and you do not reflect that fact at all in your accounting of maintenance or additions and betterments?

A. I have not undertaken to be a salesman for these things I presented today. I am trying to present the facts and the problem that confronts the trusteeship from this fiscal angle.

By Mr. McAllister:

Q. Mr. Swan, with respect to this new equipment, either on order or prospective, the terms, whether for cash or on time, either through equipment trusts or conditional [fol. 1397] sales contracts, have not been loans, have they?

A. Under our contracts for the purchase of this new equipment the manufacturer expects to get cash. Whether we pay it out of our cash resources, whether we borrow it on conditional sales contracts, or whether we borrow it on an equipment trust, is of no concern to the manufacturers.

Q. Well, that is still an open question?

A. It has not been to my mind. We plan to pay it.

Q. In cash?

A. In cash in order not to have this charge against the operations of the reorganized company. That would preclude payment of the fixed charges if the business fell off.

Q. I was just wondering whether it might not be better to defer the acceleration of the payment of the present conditional sales agreements until that question is definitely settled?

A. That question now can be settled between this date and December 1st. If the Court shall determine that we should not pay these conditional sales contracts, that is answered. If the Court instructs the Trustees to either borrow the money under conditional sales agreements or equipment trust certificates on the purchase of additional equipment, we shall do that. We had planned to try to pay for all this equipment out of the swollen earnings so as not to impair the soundness of the plan of reorganiza-

tion. It is my best judgment that if it is not done, it will very seriously preclude or impair the capacity of the reorganized road in the post-war depression to pay the fixed charges under the plan.

By Colonel Anderson:

Q. Might I ask you a question on that? You spoke of the post-war depression, of course, as prophecy? Do you [fol. 1398] not anticipate that with the very large improvements, industrial improvements and other improvements, amounting to about thirty-one plants, according to the latest you gave me I think, that the prospective earning power of this property in the future would be very considerably more than it was in the period from 1930 to 1941, which you put it awhile ago, regardless of any conditions that it would be reasonable to anticipate?

A. We are hopeful, Colonel, that the earnings will be very much better than they were in the 1930 to 1941 period, and I did not undertake to prophesy the post-war depression.

Q. Now, is it not a fact too that you may resonably expect as a result of the very considerable expenditures which have been made for improvement purposes under the management of the Trustees, that your operating conditions and expenses will be much less as a result of those circumstances than they would have been on the road before those expenditures were made?

A. We expect that to happen, and we hope to maintain an enlarged volume of traffic.

Colonel Anderson: That is all, Mr. Swan.

T. A. Thompson, being recalled as a witness on behalf of the Trustee of The Denver and Salt Lake Western Railroad Company, testified as follows:

Direct examination.

By Mr. Myer:

Q. Mr. Thompson, you are the General Auditor of The Denver and Rio Grande that testified this morning, are you not?

A. Yes, sir.

[fol. 1399] Q. Will you state to the Court the amount of rental or interest which was accrued and unpaid on the Dotsero Cutoff agreement, and also the obligations on the note of The Denver and Rio Grande, collateralizing the note of The Denver and Salt Lake Western to the amount of $3,110,000 prior to November 1, 1935?

A. As of October 31, 1935, there was accrued on the construction notes and unpaid $48,943.88, and on the collateral notes $51,462.55.

Q. Do you have that total?

A. I haven't totaled it, no.

Q. Will you state at what rate that was accrued in percentage?

A. At four per cent.

Q. Is that the rate stated in the note?

A. No, the notes were written at five per cent.

Q. Will you also state what rental or interest has been accrued upon those obligations since November 1, 1935, to January 1, 1942?

A. I can't give you the figures separate. I can give you the total figure from the date of the first default in each case; on the construction notes $1,171,039.75, and on the collateral note $1,024,434.15. That is as of December 31, 1941.

Q. Now, is that the amount accrued after November 1, 1935, or after the default occurring prior to that date?

A. That includes all matured and unpaid interest.

Q. Both before and after the petition in bankruptcy?

A. At five per cent.

Q. At five per cent?

A. At five per cent, now.

Q. What was the designation or title of the account upon which the obligations under The Denver and Salt Lake lease were carried or accrued?

A. At what time?

[fol. 1400] Q. Well, on November 1, 1935.

A. The construction Cutoff notes were interest on unfunded debt at the time, and that is a peculiar situation.

Q. Well, what was the designation of the account; the title of the account in which that was accrued on November 1, 1935?

A. What was it called?

Q. Yes.

A. Rent for leased road.

Q. And what was the designation or title of the account on which the rental or interest on the $3,110,000 was carried on November 1, 1935?

Colonel Anderson: Mr. Myer, what is the total of $3,110,000, for my information.

The Witness: There are two accounts there.

Mr. Myer: Yes. The $3,110,000 note was dated in December, 1934, and was a note of The Denver and Salt Lake Western to the Reconstruction Finance Corporation for the purpose of advancing to the D. & R. G. funds sufficient to purchase some twenty thousand odd shares of Denver and Salt Lake Railway Company stock.

Colonel Anderson: That is what I wanted to get. By the amount I didn't quite catch the note.

Q. (Question read to the witness.)

A. I am not positive. I can't answer that question positively. I think it was interest on unfunded debt.

Q. But you are not positive?

A. I am not positive.

Q. All right. Mr. Thompson, I believe you testified this morning, or do you know what the total system revenue was in 1941?

A. $31,572,624.00.

Q. Now, if you will turn to Exhibit 2, which is the con-
[fol. 1401] densed income account——

A. I have it.

Q. I believe you testified this morning that on the eight months actual and four months estimated total operating revenues of the debtor, amounting to $53,885,005, that your estimate was that thirty-three and one-third per cent of that revenue arose from traffic which went over the Dotsero Cutoff?

A. I intended to state the thirty-three and one-third per cent applied to freight traffic only.

Q. Oh, I see. Well, how much would apply to both passenger and freight?

A. Oh, a composite figure would probably be about thirty to thirty-one per cent.

Q. So, then, of the $53,885,005 total gross revenue, about

$16,000,000 would arise from traffic over the Cut-off; is that not correct?

A. That would be my estimate, yes, sir.

Q. What was the total system revenue of the debtor in the year 1932?

A. $17,560,621.

Q. What was it in 1933?

A. $17,112,794.

Q. What was it in 1934?

A. $19,246,850.

Q. When did the Dotsero Cut-off go into operation?

A. June 15, 1934.

Q. And what was it in 1935, I mean the total gross?

A. $20,944,230.

Q. So that upon the basis of your figures in the years 1932, 1933 and 1934 the total system revenue was within perhaps a million dollars of the total revenue now going over the Cut-off; is that correct?

A. Not in 1934. 1932 and 1933 within $1,000,000.

Q. Mr. Thompson, how does the amount of total revenue accruing from traffic through the Denver gateway compare [fol. 1402] with the traffic going through the Pueblo gateway, revenue east of Pueblo for delivery west of Dotsero?

A. They are approximately equal on the last study I have made on it, which was prior to this year. I have made no study of the 1942 volume.

Q. And where does the balance of this revenue come from? I mean if your statement is correct of, say, thirty per cent in the Denver and thirty per cent in this Pueblo traffic, where does the rest of it come from?

A. We get all the traffic from the southern coal field in Colorado, and all of the local traffic to Denver and Pueblo from the east, of course, via each of the other gateways, and all of our local traffic in Utah, originating in Utah, or finding destination in Utah to and from points west of the Utah common points.

Mr. Myer: I think that is all.

Cross-examination.

By Mr. McCaffery:

Q. Mr. Thompson, in accordance with my reservation this morning of a little further cross-examination, I would like

to ask you to clear up one or two points. In the first place, referring to our old friend, Exhibit 3, in this language: "Expenditures authorized or contemplated to be provided for out of cash on hand December 31, 1942," did you prepare that language?

A. No, I did not. That is the way the question was put to me as a title, and the figures below there are mine.

Q. Well, in that language why did you regard these expenditures as payable particularly out of the cash on hand December 31, 1942? Why do you feel that that cash is par-
[fol. 1403] ticularly devoted to those expenditures?

A. I don't believe that I stated that they are necessarily devoted to that cash balance. I thought Mr. Swan undertook to explain that while he was on the stand.

Q. Well, we will let it go at that, then, Mr. Thompson. Now, are you in a position to explain the situation on this depreciation of road property, as to whether you have taken it and when you are going to start taking it, and what the Commission orders on it are?

A. The Commission's orders for 1942 make depreciation of road property optional. In other words, as Auditor for the Trustees I have served notice on the Bureau of Internal Revenue that we elected to adopt depreciation on road property for the year 1942. They, in acknowledging that, incidentally verbal, by conference, stated that they would permit us to do so provided we met certain conditions imposed by them. We have not as yet determined whether or not we could meet them. We have made our study as to what the charges to depreciation of road property would be, and it is the figure that has been set up in this exhibit for, I believe it says, approximately $700,000, the annual charges for 1943, and they would be likewise approximately the charge for 1942. Now, under the Commission's order making that optional, we would not have to set that up in our expenses for 1942, although we would be permitted, if we meet the conditions of the Bureau of Internal Revenue, to charge them against our income in our income tax return.

Q. Now, I am correct, am I not, that on June 8, 1942, the Commission by order made depreciation of roadway and structures, other than track accounts, mandatory com-
[fol. 1404] mencing January 1, 1943?

A. That is correct. Next year we must charge approximately $700,000 to maintenance of way depreciation. I believe it is Account 266, a new account.

. . . . . .

[fol. 1405] WITNESS HENRY SWAN

Q. Now, in connection with your general fairness and outlook and dealing with your financial program in general you spoke of the increased possible charges and of the business conditions following the war. I want to ask you if you recall the data which you sent us at one time when the purchase of this equipment was under consideration, which consisted, I think, of a book by Mr. Sagstetter, is it?

A. Well, the information that I think you are referring to was a recapitulation of the industries on line which had been prepared by one of our traffic department.

Q. Well, that book did refer to—I don't want to put it in evidence—that contains statements substantially to the same effect. I read it with a great deal of interest. With-[fol. 1406] out asking you where those industries—for reasons familiar to us all we don't bring those questions on the record, but can you tell me the number of such industries—the number you anticipate will continue operations after the war, and the revenues anticipated therefrom during the years 1943 and 1944?

A. It is my recollection there were over thirty industries outlined that could be served either on line, or adjacent thereto or part of the through traffic over our line, of which about two-thirds would probably continue after the war was over.

Q. And could you tell me generally what was the estimated revenue which would be derived from those industries in the years 1943 and 1944? You gave me those figures, but, unfortunately, I haven't got them with me. I think it was something like $6,000,000 in 1944.

A. Well, on just two or three of these industries it is our expectation that the gross revenue would be in excess of $5,000,000.

Q. As I recall, you stated that fifty per cent of that would be net on account of the matter of the possible heavy trainloads?

A. I don't recall the statement as to that effect, but if the traffic should stay up the profit on that additional business would be high.

Q. Your percentage of your operating revenue is based upon the level of the whole business, isn't it?

A. Yes, the higher the level of traffic the bigger the recovery on the additional business.

Q. What I meant was I had these figures given to me by you, and I just wanted to get them in the record as far as I could.

A. Well, the figure you give me here in this letter was an [fol. 1407] estimate of approximately $600,000 additional business from these special industries in 1942, or about $4,000,000 in 1943, and approximately $6,000,000 in 1944.

. . . . . .

[fol. 1408] Mr. McCaffery: There is one thing that has been running through my mind, and that is the plan of reorganization is still before the Commission, and that is it will be very helpful to the Commission to have before it the matters which have been presented and the testimony which has been taken at this hearing. I am wondering whether it would be proper for me to move that the Trustees be directed by the Court to transmit a copy of the testimony and argument to the Commission for use in connection with its consideration of the plan. If any formal motion for the reopening of the record before the Com- [fol. 1409] mission is necessary for that purpose, I shall be glad to arrange for the making of such a motion. I wonder if it would not be proper for the Trustees to submit a copy of the testimony and argument to the Commission for that purpose?

The Court: If the Commission wants it you advise them, and upon their request I will send it on. We are not advised yet officially that they want it.

Colonel Anderson: You want this evidence presented certified to the Commission.

The Court: It goes into the record, and I presume they are kept advised. I presume any proceeding here, the Commission is at once advised.

Mr. McAllister: Yes, they are furnished with the record and the proceeding. I might ask if Your Honor wants the testimony here transcribed and placed in the record.

The Court: What would you advise?
Mr. McCaffery: I might say I am ordering a copy.

OPINION

The Court: On October 17, 1942, the Insurance Group Committee, so-called, representing institutions holding minority interests in various bond issues of this debtor, and certain indenture trustees of the mortgages on the debtor's property, excepting the general mortgage, filed a petition praying for an order directing the trustees to pay interest on bonds and notes of the debtor in an amount of $2,481,812.52, to be divided among the respective issues and the Reconstruction Finance Corporation in accordance with the allocations of new securities set forth in the proposed plan [fol. 1410] of reorganization approved by the Interstate Commerce Commission on July 13, 1942, known as the Commission plan, which provides that interest shall be paid on the new bonds therein provided for when issued, from January 1, 1942.

The same parties also filed on the 23rd of October, 1942, a motion to restrain the Trustees from any redemption, prepayment or other satisfaction before maturity of the principal of any obligations incurred by them, including the deferred payment of the purchase price of equipment, or any other long term obligation incurred by the Trustees, and to withdraw any notice of such redemption, prepayment or satisfaction, if any has been given, and further directing the Trustees to set aside cash in special trust accounts equal to the total amounts to become payable by the reorganized company on all securities issued or assumed by it pursuant to the reorganization plan approved by the Commission under date of July 13, 1942, as if such plan had been consummated on January 1, 1942, and that withdrawals from such funds shall be made only for the purpose of paying accrued interest on the new securities provided for in such plan, or existing securities.

An answer and objections to said motion were filed by the Trustee of The Denver and Salt Lake Western Railroad Company and by the Reconstruction Finance Corporation. The motions were heard and argued on the 23rd and 24th of October, 1942, at the conclusion of which the Court denied the petitions, stating it would file a memorandum opinion.

[fol. 1411] It will be observed that the moving parties asked to have interest paid in proportions allocated according to the proposed plan of reorganization of the Interstate Commerce Commission of July 13, 1942. It is novel that these parties should recognize and rely upon this proposed plan in view of the fact that the said plan has not been finally approved by the Commission, and not certified to this Court for its consideration as required by the Bankruptcy Act. Further, these moving parties have filed objections to said plan with the Commission and are pressing the same, and, if defeated there, it may be assumed that they will renew their objections when the matter comes before this Court, and may later vote against it if it is approved and submitted to the securityholders in accordance with the Bankruptcy Act.

This plan of the Interstate Commerce Commission referred to is the third that has been promulgated. The first proposed by the Commission was strenuously opposed by the proponents of these motions and other interested parties before the Commission and this Court, and after full hearing was rejected by the Court and returned to the Interstate Commerce Commission with the Court's own suggested plan. The latter was not approved by the Commission. The Interstate Commerce Commission thereafter held further hearings, and put out the plan referred to of July 13, 1942, which these moving parties are on record as objecting to. For the reasons stated there is no certainty that the said plan will ever be adopted or become effective, and we have no reason to assume for the purposes of this motion or otherwise that this plan and its allocation of new [fol. 1412] securities will ever be finally adopted or approved by the Commission, the Court, and the securityholders.

This is the fourth time that this property has been in the hands of this Court in bankruptcy, the second time under the present judge.

This motion indicates that these creditors have not learned the lesson indicated by the past history of the property, which demonstrates that its financial difficulties have been due primarily to the insistence, by the bondholders and their trustees, upon the payment of interest on watered securities, even though not earned. This particular reorganization proceeding was precipitated by the fact that the

debtor, in order to stave off bankruptcy, borrowed from time to time just before bankruptcy over $12,000,000 from the Reconstruction Finance Corporation for the following purposes; to pay one or more unearned installments of interest on its Consolidated and Underlying Mortgages, interest on its Refunding and Improvement Mortgage, and to purchase certain ties the debtor had under contract. It borrowed further funds from the Reconstruction Finance Corporation to pay interest on its General Mortgage, and current taxes due the State of Colorado for two succeeding years. And later the debtor secured further loans from the Reconstruction Finance Corporation to construct the Denver and Salt Lake Western—otherwise known as the Dotsero Cut-off. In addition it caused the Reconstruction Finance Corporation to make loans to The Denver and Salt Lake Western Railroad Company, which the latter, in turn, loaned to the debtor to acquire the control of The Denver [fol. 1413] and Salt Lake Railroad—otherwise known as the Moffat Road.

The only criticism that can be made of the Reconstruction Finance Corporation is that it loaned money to this debtor when it was bankrupt, thus enabling it to stave off bankruptcy and make its financial condition worse when it finally came into court. In view of this it is hard to understand the present hostility that these moving parties have shown to the Reconstruction Finance Corporation as a creditor, or explain the conflicting views each takes on the controversial points that have arisen in the course of this proceeding.

This particular motion was precipitated evidently by the plans of the Trustees, Mr. McCarthy and Mr. Swan, to pay out of cash on hand $2,282,106.00 of Trustees' obligations representing the balance due on certain Diesel engines and switchers; five steam locomotives and three Diesel freight locomotives, and to pay cash for certain equipment on order and soon to be delivered.

It is true, as argued, that during the last year and a half the earnings of this property have increased out of all proportion, and show a greater per cent of increase than any other Class 1 railroad in the Western territory. The gross for the current year it is estimated will be over $50,000,000.00 as against $31,000,000.00 for 1941.

The financial program of the Trustees to which objection is made is as follows:

[fol. 1414] Estimated cash balance January 1, 1943, before payment of conditional sales agreements		$10,057,000
Requirements:		
Balance (Dec. 1, 1942) on conditional sales agreements as follows:		
Electro-Motive Corporation (assigned to Omaha National Bank) covering one 1,000 h.p. Diesel switcher purchased to serve Denver Ordinance Plant	$62,057	
Northern Trust Co., Chicago, covering 13 Diesel switchers acquired summer of 1941 to handle increased business account defense effort	545,318	
Baldwin Locomotive Works (assigned to City National Bank and Trust Co., Chicago), covering 5 steam locomotives acquired 1941 and being amortized as Defense Project under War Dept. Necessity Certificate WD-N-3303	710,370	
Electro-Motive Corporation (assigned to First National Bank of Denver), covering three 5400 h.p. Diesel freight locomotives acquired 1941 and being amortized as Defense Project under War Dept. Necessity Certificate WD-N-3303	964,361	2,282,106
Equipment on order:		
Six 5400 h.p. Diesel freight locomotives being built by Electro-Motive Division, General Motors Corporation, to handle traffic developed by Defense Plant Corporation (Columbia Steel) steel mills near Provo, Utah, covered by Rio Grande Purchase Order 7051, 2-17-42. (Delivery, originally scheduled for Sept.-Oct., 1942, postponed because locomotive plant capacity being devoted to Navy orders)		3,044,746

1,000 70-ton gondolas to handle Provo Steel traffic, Rio Grande Order 12283 7-3-42 (Supplemented 9-29-42) (780-'42 220-'43)	3,582,300
300 Dump cars to be acquired for handling of limestone and dolomite to new steel mills near Provo (Not ordered but desired at once and trying to get secondhand. Offer made to purchase 160 at 1,500.00.)	990,000
Cash required to complete work authorized by Court but not yet performed	3,700,000
Estimated 1942 Income Tax Payments	1,300,000
Cash working fund required	1,250,000
Total Cash Requirements	$16,149,152

[fol. 1415] All of this equipment is necessary, in the opinion of the Trustees, for the proper operation of the property under war conditions, to serve promptly and efficiently the many government war plants established on the line of this railroad, as well as the tremendous increase in bridge traffic consisting of thousands of troops and quantities of war munitions en route to the Pacific Coast and in the opposite direction. Most of this equipment has been ordered at the special request of the government. Washington has told the Trustees just how much equipment they must have, for instance, to serve the new Columbia Steel Plant being built on the line of this railroad near Provo, Utah, and also that 2,000 new cars are necessary to haul coal from Utah to the new steel plant in southern California.

The moving parties objecting say:

> "No avoidable payments should be made, particularly any retirement before maturity of equipment obligations for the payment of which at maturity funds will be provided through charges for equipment depreciation, in such manner as to prejudice the payment in 1942 of such accruals of interest under the Commission Plan."

It is the view of the Court and its Trustees that these greatly increased earnings—which it is said justify the payment of the interest—are the direct result of the present

war emergency. Conservative management and business principles dictate that all expenditures incurred to provide the necessary facilities to handle this increased business should be paid from such revenues and not passed on as a debt to the new corporation when it takes over the property under the reorganization.

It is true, as alleged, that $30,000,000 has been paid out [fol. 1416] in rehabilitation of right-of-way, shops and equipment. To some of these expenditures the parties have from time to time objected. The tremendous business this property is now doing as a transcontinental carrier of war material and troops has amply justified these expenditures as well as the Trustees' financial policy.

The duty of the Court in this respect is stated by the Court of Appeals in Van Schaick v. McCarthy, 116 Fed. 2d, 987, in which the propriety of some of these expenditures was raised, the Court saying at page 983:

> "During that period the railroad company must be operated by the trustees under the supervision and control of the court in the public interest and for the protection of the private interests involved, and to that end such expenditures must be made as are reasonably necessary to preserve and protect those interests and maintain the integrity of the railroad, so that it may be turned over to the reorganized company as a going concern. Sec. 77 contemplates that the reorganized road shall be a living, not a dying, railroad enterprise. To permit the competitive position of the road to be lost during the period of reorganization would greatly endanger the future earnings upon which the plan is to be largely based and out of which the reduced fixed charges are to be paid."

The expenditures proposed (supra) are reasonable and necessary to preserve and protect the interests of the securityholders, and maintain the integrity of the railroad as a going concern so that it may be turned over to the new company in reorganization as a going concern. But there is the additional reason at this time, to wit, the duty of this railroad as a transcontinental transportation facility under war conditions to meet the demands of the Government. The demand is that the Trustees borrow the money to pay [fol. 1417] for new equipment rather than to pay for it out of cash on hand and thus save over $100,000 in interest.

If this equipment is purchased and paid for in full, after reorganization is completed the new owners can still use it as collateral for further loans.

It is also urged that the estimated cash balance of $10,057,000 as of January 1, 1943, can be safely distributed at this time. Sight is lost of the fact that the first six months of every year have been the lowest in the earnings of this property. It has always been necessary to carry over January 1st of each year a large cash balance to meet taxes due the last of February, to complete improvement work already authorized by the Court and not yet performed, and to meet other large expenditures during the first six months of the year when earnings are small.

The motion and the argument in support thereof disclose a marked cleavage between the business policies of the Trustees and these creditor institutions. The Court believes in old-fashioned finance, desiring to pay its own obligations incurred during trusteeship and those resulting from the war emergency ahead of interest on defaulted obligations which the Court inherited, and while these revenues exist. It would thus trim its sails and be in as safe a financial condition as possible when the inevitable slump comes as it is bound to within the next few years.

Mr. Justice Hughes, in Carpenter v. Wabash Ry. Co., 309 U. S. 23, at 27-28, said:

> [fol. 1418] "We have held that earnings, while a railroad is in possession of the court and operated by its receivers, 'are not necessarily and exclusively the property of the mortgagees' but are subject to the payment of claims which have superior equities as they may be found to exist," citing authorities.

Furthermore, the granting of this motion would open the gateway to a flood of applications for the diversion of these swollen earnings, such as the payment of rent due the Reconstruction Finance Corporation for the use of the Denver and Salt Lake Western (the Cut-off), and likewise rent on the Junction railroad, and many other pending claims now quiescent. The Court is also informed that payment of past due interest would raise a very serious income tax situation which cannot be determined with any degree of exactness in advance.

Counsel strongly urge the Court to defer its judgment to that of these trustee institutions of New York, emphasis

being laid upon their experience and judgment in large financial affairs, especially railroads. This brings to mind the fact that it is some of these same trustees who have dictated the policy of this railroad, and are responsible for the money borrowed to pay interest not earned and current expenses such as taxes already referred to. Millions of dollars have been borrowed by the Trustees during the seven years they have been in charge of this property. Their obligations have been met with such promptitude, often in advance, as to establish in the money markets of the country such a credit rating that when they need temporary funds, unlike other roads in reorganization, they are able to borrow money without resort to any of the lend-
[fol. 1419] ing agencies of the Federal Government, to none of which are the Trustees at present indebted. Before this railroad came into the hands of the Court, it borrowed money on equipment obligations at the rate of five to five and a half per cent, while the Trustees have borrowed several millions of dollars on Trustees' certificates at the rate of three and a quarter per cent and some as low as two per cent and less.

A somewhat similar question was presented to Judge Davis of the District Court of St. Louis (who has had perhaps more experience in railroad reorganizations than any other Federal judge) in the matter of the St. Louis & Southwestern Railway Company, 17 Fed. Sup. 68. The question there was that the trustees asked authority to make certain expenditures to build and purchase new engines and passenger coaches, and the railroad trustees, as here, desired to pay for it in cash. The trustees under three general mortgages of the company asked that the railroad trustees be directed to negotiate equipment trust certificates for the financing thereof, and at the same time petitioned for the payment in cash of certain defaulted interest installments under the railroad's second mortgage income bond certificates. The debtor deemed that the trustees' cash position and its present and prospective earnings fully justified the expenditure of cash for the building of the locomotives and the purchase of the coaches. The Court held, first, that it was without authority to increase indebtedness in reorganization proceedings by authorizing the issuance of additional securities, stating the Bank-
[fol. 1420] ruptcy Act does not contemplate such an action

unless it is essential for the continued operation of the railroad as a common carrier, and, further, that the custom of railroad financing whereby railroad equipment is ordinarily financed through equipment trust issues was insufficiently persuasive to authorize the trustee of a railroad in reorganization to finance necessary equipment where the trustees had sufficient cash with which to pay for the equipment. The Court further held that current expenses arising out of operation of the business constitute claims prior to those of the bondholders, and must be paid by the bankruptcy trustee out of available funds, and, finally, that trustees of the railroad in reorganization would be allowed to finance essential equipment out of cash available rather than by issuing trust equipment certificates so that a portion of the cash could be used to pay defaulted bond interest, since, under the rule which makes claims for operating expenses during receivership prior to bondholders' claims, expenditures, though chargeable to capital account, are entitled to some preferred status. And, finally, that the District Court in which the railroad has filed a petition for reorganization should not, in exercising its discretion, increase the indebtedness which the railroad seeks to decrease; but, where cash is on hand to pay for necessary additions and replacements, the Court should authorize expenditure of such cash for such purpose.

[fol. 1421] On appeal the Circuit Court of Appeals of the Eighth Circuit affirmed (Bankers Trust Co. v. Henwood, 88 Fed. 2d, 163). The Court, speaking through Judge Stone, held that an order of the District Court in a corporate reorganization proceeding, authorizing the trustee to purchase rolling stock for cash, was made in the exercise of discretion which could not be reviewed. In the case at bar, as in that case, the Court is really asked to incur additional indebtedness by the issue of equipment certificates in order that cash in the hands of the Trustees may be used to pay interest on defaulted obligations. In the Circuit Court of Appeals the appellants took exception to the following from Judge Davis' opinion:

> "The debtor came into this court to reduce its debts through a plan of reorganization. Certainly the approval of a new form of indebtedness, which almost of necessity must be binding on the successor or reorganized company, thereby increasing the funded debt,

> when the trustee has or will have sufficient cash on hand to pay for the essential equipment, is within neither the letter nor the spirit of the law."

Asserting a custom of long standing whereby railroad equipment is ordinarily financed through equipment trust issues the Court of Appeals observed: "There is no authority to the effect that equipment must be so financed, and the fact that such procedure is customary, if that be the case, is not sufficiently persuasive to alter the equities or logic of the situation."

In Southern Railway Co. v. Carnegie Steel Co., 176 U. S. 257, the Supreme Court observed that they had refrained from laying down any rule controlling in every case, involving the rights of unsecured creditors of a corporation in the [fol. 1422] hands of a receiver to have their demands paid out of net earnings in preference to mortgage creditors, stating:

> "But it may be safely affirmed upon the authority of former decisions that a railroad mortgagee when accepting his security impliedly agrees that the current debts of a railroad company contracted in the ordinary course of its business shall be paid out of current receipts before he has any claim upon such income; that, within this rule, a debt not contracted upon the personal credit of the company, but in order to keep the railroad itself in condition to be used with reasonable safety for the transportation of persons and property, and with the expectation of the parties that it was to be met out of the current receipts of the company, may be treated as a current debt."

This would seem to be ample justification for the policy of the Trustees who in their discretion wish to finance current needs for equipment and improvements out of the earnings as far as they will go. It would seem to be a matter of discretion which the Court should not interfere with, especially when, as here, the moving parties acquiesce in the views of the Trustees as to the necessity for this new equipment.

The Court, from its own knowledge of this property and its physical needs, knows that as a result of the tremendous business the property is now doing, there is a constant and

enormous depreciation in the rolling stock and right-of-way. This is especially true of the motive power evidenced by the fact that engines are now turned about at terminals and sent out again without proper time for shopping and maintenance repairs. Further, in order to handle the business [fol. 1422a] the Trustee have leased from other railroads eighteen locomotives. Before long it will be necessary to authorize another budget of expenditures for improvements to take care of this wear and tear that the roadway and its equipment is being subjected to, and which it is impossible to renew due to the number of trains passing over the line and priority requirements for materials.

In conclusion, I am of the opinion that the Trustees have not abused their discertion in the use they propose to make of current earnings. The motions should be and are denied.

[fol. 1423] In the District Court of the United States Within and for the District of Colorado, Sitting at Denver

No. 8669

In the Matter of the Denver and Rio Grande Western Railroad Company, Debtor

In Proceedings for the Reorganization of a Railroad

Excerpts from Hearing of April 14 to 16, 1943

Petition and Supplemental Petition of the Trustee of The Denver and Salt Lake Western Railroad Company for Payment of Rental by The Denver and Rio Grande Western Railroad Company, and Petition of the Moffat Tunnel Improvement District in Support Thereof

Be It Remembered that on, to wit, the 14th day of April, A. D. 1943, the same being one of the regular juridical days of the November term, A. D. 1942, of said court, this cause came on for hearing before the Honorable J. Foster Symes, Judge of the District Court of the United States for the District of Colorado, on the petition and supplemental petition of the Trustee of The Denver and Salt Lake Western Railroad Company for payment of rental by The Denver and Rio Grande Western Railroad Company, and peti-

tion of the Moffat Tunnel Improvement District in support thereof.

[fol. 1424] APPEARANCES:

George D. Gibson, Esq., of the firm of Hunton, Williams, Anderson, Gay & Moore, of Richmond, Virginia, and William W. Grant, Esq., and Morrison Shafroth, Esq., of the firm of Grant, Shafroth & Toll, for the Insurance Group Committee.

Messrs. Henry McAllister, Thomas R. Woodrow, and John L. J. Hart, for the Trustees of the debtor, The Denver and Rio Grande Western Railroad Company.

William V. Hodges, Esq., of the firm of Hodges, Vidal & Goree, for the debtors, The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company.

Erskine R. Myer, Esq., for H. Allyn Hicks, Esq., Trustee of the debtor The Denver and Salt Lake Western Railroad Company and the Moffat Tunnel Commission.

Mason A. Lewis, Esq., of the firm of Lewis & Grant, for the Chase National Bank of the City of New York, as Trustee.

Robert G. Bosworth, Esq., of the firm of Pershing, Bosworth, Dick & Dawson, for the Guaranty Trust Company of New York, as Trustee.

Messrs. Langdon H. Larwill and Daniel K. Wolfe, of the firm of Lindsey & Larwill, for the United States Trust Company of New York, as Trustee.

Miss Norma L. Comstock and Norman H. Comstock, Esq., for the Central Hanover Bank and Trust Company, as Trustee.

Emmet McCaffery, Esq., counsel, James L. Homire, Esq., special counsel, and James A. Marsh, Esq., for the Reconstruction Finance Corporation.

[fol. 1425] Messrs. Peter H. Holme and Milton J. Keegan, of the firm of Dines, Dines & Holme, for the City Bank Farmers Trust Company, as Trustee.

C. H. Anderson, Esq., Assistant Attorney General of the State of Colorado.

Richard K. Paynter, Jr., Esq., for the New York Life Insurance Company.

Eugene A. Schmidt, Jr., Esq., for the Metropolitan Life Insurance Company.

William J. Kane, Esq., for the Railroad Credit Corporation.

J. Fred Schneider, Esq., for the Untermeyer Family Group.

. . . . . .

[fol. 1426] HENRY SWAN, a witness called and sworn on behalf of the Trustee of the debtor, The Denver and Salt Lake Western Railroad Company, testified as follows:

Direct examination.

By Mr. Myer:

(Thereupon documents were marked for identification Insurance Group Exhibits 1, 2, 3, 5 and 6.)

Mr. Myer: By stipulation of counsel, Insurance Group Exhibits 1, 2, 3, 5 and 6 are offered in evidence. Do you want to see these, Mr. McCaffery?

Mr. McCaffery: I want a copy of them.

. . . . . .

[fol. 1427] T. A. THOMPSON, a witness called and sworn on behalf of the Trustee of the debtor, The Denver and Salt Lake Western Railroad Company, testified as follows:

Direct examination.

By Mr. Myer:

Q. Will you state your name?

A. T. A. Thompson.

Q. What position do you occupy with the debtor?

A. General auditor.

Q. How long have you occupied that position, Mr. Thompson?

A. Since July 1, 1937.

Q. And you are presently occupied in that capacity?

A. Yes, sir.

[fol. 1428] Q. I hand you a document marked Salt Lake Western Exhibit 1. I will ask you if that was prepared in your office, and ask you to state what it is.

A. It was prepared in my office, and is a general balance sheet of The Denver and Rio Grande Western Railroad Company as of December 31, 1942.

Q. That statement accurately reflects the accounts and records in your office, does it?

A. It does.

Mr. Myer: I offer in evidence S. L. W. Exhibit 1.

Q. Mr. Thompson, I hand you a document marked S. L. W. Exhibit No. 2, and ask you to state what that is.

A. The condensed income account of The Rio Grande Western Railroad for the year 1942 and two months of 1943.

Q. Will you state what that exhibit shows as to the total operating revenues of The Denver and Rio Grande for the year 1942, and also the net?

A. Total operating revenues are $54,475,496.76.

Q. What is the net?

A. Net income $11,306,965.60.

By the Court:

Q. How is that; after all fixed charges?

A. That is after all fixed charges.

(Thereupon a document was marked for identification S. L. W. Exhibit No. 3.)

By Mr. Myer:

Q. Mr. Thompson, I hand you a document marked S. L. W. Exhibit 3, and ask you to state what that is.

A. It is a statement of freight traffic and system revenues thereon moved via the Dotsero Cut-off for the years 1937 to 1942, inclusive.

Q. Will you read the item "Per Cent of System Revenue [fol. 1429] Accruing On Business Moving Over or Via the Dotsero Cut-off" at the bottom of the page in each of the years 1937 to 1942?

A. 1937, 25.02 per cent; 1938, 27.44 per cent; 1939, 28.52 per cent; 1940, 29.05 per cent; 1941, 31.43 per cent; and 1942, 33.79 per cent.

Q. Was that instrument prepared in your office?

A. It was.

Q. Does it accurately reflect the figures that appear upon the accounts and records of The Denver and Rio Grande?

A. As near accurate as we could make it.

(Thereupon a document was marked for identification S. L. W. Exhibit 4.)

Q. Mr. Thompson, I hand you a photostatic copy of a document, the copy being marked S. L. W. Exhibit 4, and ask you if that document was prepared in your office from the books and records of the Denver and Rio Grande Railroad?

A. It was.

Q. Will you state what that exhibit purports to show?

A. Payments by the Rio Grande Western Railroad to The Denver and Salt Lake Railway Company in connection with joint operation between mile post 1.5 on the northwestern terminal and Orestod for the calendar years 1936, 1937, 1938 and 1939.

Q. Do you know, and if you do know, will you so state, whether or not the obligations of the Denver and Rio Grande under the Joint Trackage Agreement with the Denver and Salt Lake have been paid in full to date?

A. They have.

Q. This exhibit, as I understand it, shows the amounts of those payments in the years 1936, 1937, 1938, and 1939, does it not?

A. It shows the amounts charged in those years. The payments may have overlapped a little bit.

(Thereupon a document was marked for identification S. L. W. Exhibit 5.)

[fol. 1430] Q. Mr. Thompson, I hand you a photostatic copy marked S. L. W. Exhibit 5, and ask you if you can identify that, and what it purports to show?

A. It is the continuation of the previous exhibit, covering the years 1940, 1941 and 1942.

Q. Will you state the total amounts charged or paid in the years 1940, 1941 and 1942 by the Denver and Rio Grande to the Salt Lake under the terms of the Trackage Agreement as shown by that exhibit?

A. For the year 1940, $867,607.00; for the year 1941, $995,307.00; for the year 1942, $1,295,300.00.

Q. Mr. Thompson, have you prepared an exhibit or are you able to testify regarding what amount of cash of the Denver and Rio Grande has been used since the October hearing of 1942 for the purchase of equipment obligations as then contemplated?

A. I have data with me that will enable me to answer your question I think.

Q. Can you give us a statement of the cash on hand on December 31, 1942, of the Denver and Rio Grande?

A. Nine million eight hundred fifty-nine thousand five hundred and nine dollars and fifty-six cents.

Q. Have you a statement of cash on hand of the Denver and Rio Grande at the present time?

A. As of the close of March 31st the balance was $13,488,418.47.

By the Court:

Q. Was that after all your taxes had been paid?

A. No, all the taxes have not been paid. There is a lot of taxes yet to pay.

Q. You mean federal taxes and Colorado?

A. Colorado taxes due on February 28th have been paid.

Q. No income tax?

[fol. 1431] A. We paid our first quarter of federal, Colorado and Utah. Out of that March 31st—the Colorado was not paid out of that March 31st balance, however. That was paid since then.

Mr. Myer: I think that is all.

Cross-examination.

By Mr. McCaffery:

Q. Mr. Thompson, following up what Mr. Myer was just asking you about, at the hearing regarding the payment of interest in October, 1942, you presented, did you not, a statement showing the amount of cash which was anticipated would be on hand on December 31, 1942, and what commitments there might be against that cash?

A. I did.

Q. Have you or can you in effect bring that statement down to date? That is, can you tell us which of those uses have now been taken care of, and also what commitments you feel there are against the present cash?

A. I will give commitments of the same character. I don't know as I can make any statement on all commitments.

Q. And so that we may be clear on the relation of that exhibit to this one, will you state which of the commitments that were then spoken of have now been disposed of?

A. Well, we paid off on December 1st the conditional sales agreements amounting to $2,282,106.00. That is the principal amount of those agreements outstanding on that date, and as of March 31st we have paid out $792,006.00 for the

purchase of 221 of 1,000 freight cars. We had likewise paid approximately $450,000.00 in 1942 ad valorem taxes payable this year. We have also paid the last quarter of railroad unemployment taxes, and have paid the first quarter [fol. 1432] of income taxes, aggregating $2,180,000.00. That is federal and state income taxes. Actually we have paid more than that on the income taxes for the reason that we have purchased tax notes to the extent of $1,600,000.00, of which we still have $1,200,000.00 on hand.

Q. Those are the commitments to which you referred last October that have now been disposed of?

A. Yes.

Q. What do you feel are the commitments now existing against the persent cash in a similar way?

A. Well, we still have on order the six Diesel freight locomotives to cost approximately $3,044,000.00, the balance of the order for 1,000 freight cars which means approximately $2,750,000.00 yet to pay, and we have on order 250 ton flat cars estimated to cost $715,000.00, and ten Diesel electric switching locomotives estimated to cost $785,000.00.

By the Court:

Q. Have you steam locomotives on order?

A. The steam locomotives are on order, but are to be paid for by Defense Plant Corporation and leased to The Denver and Rio Grande. Well, we still have, of course, the uncompleted portion of our improvement program. I can't tell you what that amounts to.

By Mr. McCaffery:

Q. Are you informed, Mr. Thompson, as to what are the present practical possibilities of your securing the freight equipment and locomotives which you referred to, that is, whether you are actually going to get them?

A. As is the case with most equipment, I certainly am not in a position to make a positive statement we are going to get them.

Q. For instance, with regard to those ten Diesels, Mr. [fol. 1433] Thompson, am I correctly informed that you expect to actually get about three of those in the reasonably near future?

A. Are you talking of the ten switching locomotives?

Q. The ten Diesels you spoke of.

A. We have only six of those contemplated, and three of those, my latest information is, are to be delivered in April and May. The switching locomotives, two of them have been delivered just within the past ten days, and the other eight I believe are coming.

Q. Now, the Court referred, Mr. Thompson, to steam locomotives being acquired with the cooperation of the Defense Plant Corporation. I believe that the terms of that arrangement have been covered in a recent petition and order by the Court in these proceedings; is that correct?

A. I believe there was an order entered on April 9th, authorizing the execution of the lease and agreement.

Q. I believe Mr. Myer put in the record as part of the Salt Lake Western Exhibit 1 the earning statement of the Denv and Rio Grande for the two months of January and February, 1943. Are you in a position to advise us what the earnings for the month of March were, or have they been computed?

A. We have nothing but our preliminary estimates, and they show a net income of approximately $900,000.00 for the month of March.

Q. Can you tell us, Mr. Thompson, how the months of January, February and March, 1943, compare with the months of January, February and March, 1942?

A. You mean gross?

Q. Well, I had in mind net, but either gross or net or both I think will give us the comparison.

[fol. 1434] A. I can give you the gross figures. I don't have any net figures of the property. The gross revenues for the first two months show an increase of $4,122,410, or 68.39 per cent, and for the month of March the estimated revenue is $5,835,000, and I haven't figured the per cent increase, but I believe it is 69.

Q. One other minor point, Mr. Thompson. I believe in the October, 1942, hearing some reference was made to the fact that the Commission has required, beginning January 1, 1943, that depreciation be accrued on certain fixed assets, and at that time you stated that you estimated the amount of such depreciation would run about $700,000 a year. Is that still a fair estimate?

A. Yes. A little bit higher.

Q. Take the January, February and March, 1943 figures which you have given us, do they include a monthly accrual for that item?

A. They include an expense accrual for depreciation of road property.

Q. How about the year 1942? I believe you testified that you had an optional possibility of taking it for that year. Did you in fact take it, and did the 1942 earnings which you have given us include that?

A. We didn't take it, and therefore they do not reflect any charges to depreciation on road property.

Mr. McCaffery: If Your Honor please, there are one or two additional minor exhibits which I may need Mr. Thompson to identify, which are not at the moment available, but I presume Mr. Thompson will be available perhaps later in the day. Thank you, Mr. Thompson.

Redirect examination.

By Mr. Myer:

Q. All of these exhibits from 1 to 5, which I have shown [fol. 1435] you, Mr. Thompson, were prepared in your office and under your direction, were they not?

A. They were.

Mr Myer: We offer in evidence S. L. W. Exhibits 1 to 5. I think that is all.

Cross-examination.

By Mr. Gibson:

Q. Mr. Thompson, I am told that the Interstate Commerce Commission has recently extended in large measure the emergency rate increases?

A. I have nothing except what I have seen in the papers on it up to this time.

Q. Would you be able to tell us the approximate amount, what that would mean on the basis of 1942 effective of that year?

A. That would have been effective—I have a close figure on the amount of those increases for the part of 1942 that they were effective, and that was approximately $2,000,000.00. I am speaking of the freight increases only, not the passenger increases, and on the basis of the revenue at its present scale, and eliminating the figures on an annual basis, would affect the Rio Grande somewhere between two and a quarter and two and three-quarter million dollars.

By Mr. McCaffery:

Q. Is that gross or net, or before the net income tax?

A. That is gross. We are in the income tax bracket now, subject to income tax.

By Mr. Gibson:

Q. What is the amount of the federal income tax liability disclosed in your income tax return filed on March 15th of this year?

A. I don't have it with me, but the figure is approximately $1,760,000.00.

[fol. 1436] Q. Have you any estimate what that figure will be in respect of 1943?

A. No estimate for the full year. We accrued $900,000.00 for the first two months of the year.

Q. Whatever basis you used in that accrual, followed for the full year, what would the total accrual for the full year be?

A. $5,400,000.00.

Q. So far as your estimate is now available, that is the presumptive range?

A. I have no idea what the revenue is going to be for the balance of the year. That is just taking the net taxable income for the first two months, and that is a round figure, of course.

Q. Is there now pending in respect to the Rio Grande an application for wage increases?

A. As regards the Rio Grande and all other railroads, yes, sir.

Q. Can you tell us approximately what is the total amount per year that is involved in that issue to the Rio Grande?

A. On the full demand?

Q. Yes.

A. Three and a half to four million dollars.

[fol. 1437] By Mr. Schneider:

Q. The $900,000 which you have set up for accrued taxes, does that include the income taxes for the States of Colorado and Utah?

A. It does not. It is purely an estimate, and is based on approximately 40% of our net income subject to Federal taxes.

Q. That is only for Federal taxes?
A. That is right.

[fol. 1438] L. L. PRATER, a witness called and sworn on behalf of the Trustee of the debtor, The Denver and Salt Lake Western Railroad Company, testified as follows:

Direct examination.

By Mr. Myer:

Q. Will you state your name?
A. L. L. Prater.
Q. Are you employed by The Denver and Salt Lake Railway Company?
A. I am.
Q. In what capacity?
A. Auditor.

The Court: What?
The Witness: Auditor.

Q. How long have you been so employed?
A. Since May, 1932.
Q. You are presently engaged in that occupation?
A. That is right.
Q. Mr. Prater, I hand you a document marked S. L. W. Exhibit 6, and ask you if you know what that is, and state what it purports to show.
A. It is a daily cash statement of the Denver and Salt Lake Railway Company for April 6, 1943, showing the net cash balance as of that date.
Q. Will you state what that net cash balance is shown to be?
[fol. 1439] A. $156,292.07.

The Court: Is that cash on that particular day?
The Witness: Yes, sir.

(Thereupon a paper was marked for identification as S. L. W. Exhibit 7.)

Q. Mr. Prater, I hand you a document marked S. L. W. Exhibit 7 and ask you if you can identify that, what it is?

A. This is a statement of income, profit and loss, and general balance sheet of The Denver and Salt Lake Railway Company as of December 31, 1942.

The Court: That is for a year, is it?

The Witness: That is for the year ended December 31, 1942.

The Court: All right.

(Thereupon a paper was marked for identification S. L. W. Exhibit 8.)

Q. Mr. Prater, I hand you a document marked S. L. W. Exhibit 8, and ask you to identify that and state what it purports to show.

A. This is a statement of the income account for the twelve months ended December 31, 1942, for The Denver and Salt Lake Railway Company.

Q. Will you state what that exhibit shows in reference to the gross income of The Denver and Salt Lake Railway Company?

A. The gross income for the year 1942 was $2,880,758.56.

Q. And the total, or, rather, the net income?

A. The net income was $83,909.68.

Q. Now, is that after payment of bond interest and taxes and other fixed items?

A. Yes, sir.

(Thereupon a paper was marked for identification [fol. 1440] S. L. W. Exhibit 9.)

Q. Mr. Prater, I hand you a document marked Salt Lake Western Exhibit 9, and ask you to identify that and state what it purports to show.

The Court: This is Salt Lake Western?

Mr. Myer: This is Denver and Salt Lake.

A. This is a statement of the income account of The Denver and Salt Lake Railway Company for the month of January, 1943.

Q. Will you state what the exhibit shows as the total operating revenues?

A. The total operating revenues were $296,155.18.

Q. And the net income?

A. $82,402.16.

Q. That is for the month of January, 1942?

A. 1943.
Q. 1943?
A. Yes, sir.

(Thereupon a paper was marked for identification S. L. W. Exhibit 10.)

Q. Mr. Prater, I hand you a document marked S. L. W. Exhibit 10, and ask you to identify it and state what it is, and what it purports to show.

A. This is a statement of The Denver and Salt Lake Railway Company, showing the income account for the month of February, 1943, with a total operating revenue of $262,911.88, and the net income $83,911.60.

Q. Is that after provision for taxes and bond interest and other fixed items?

A. Yes.

(Thereupon a paper was marked for identification S. L. W. Exhibit 11.)

Q. Mr. Prater, I hand you a document marked S. L. W. Exhibit 11, and ask you to identify it and state what it [fol. 1441] purports to show.

A. This is a statement showing the amounts expended under Article III of the Joint Trackage Agreement between The Denver and Salt Lake Railway Company and The Denver and Rio Grande Western Railroad Company, dated October 15, 1928. It shows the amount of money that has been expended under that article of the Joint Trackage Agreement, in the amount of $1,133,754.22.

Q. Do you know the total amount of obligations in money called for by that article?

A. $1,250,000.

Q. Then, of the amount of $1,250,000, the limit stated in Article III, the Denver and Salt Lake has expended $1,133,754.22, in compliance with that article, is that correct?

A. That is right.

(Thereupon a paper was marked for identification S. L. W. Exhibit 12.)

Q. Mr. Prater, I hand you a document marked Salt Lake Western Exhibit 12——

The Court: You are saying Salt Lake Western, is that right?

Mr. Myer: Yes, the exhibit number.

Q. —Salt Lake Exhibit 12, and ask you if you know what that is and can identify it and state what it purports to show.

A. This is an excerpt from the minutes of the meeting of the Board of Directors of The Denver and Salt Lake Railway Company held on February 23, 1943, wherein the interest payable on the income mortgage bonds was declared to be six per cent.

Q. Was there an authorization for the payment of this interest?

A. There was.

[fol. 1442] Q. Was it paid?

A. It was.

Q. Will you state the total amount of The Denver and Salt Lake income bonds outstanding?

A. $11,000,000.

Q. Even?

A. Even.

Q. Mr. Prater, these exhibits which I have handed you, S. L. W. Exhibits 6 to 12, inclusive, were prepared in your office and under your supervision and at your direction?

A. Yes, sir.

Q. Do they correctly reflect the data and information upon the books of The Denver and Salt Lake Railway Company?

A. They do.

Mr. Myer: I offer in evidence S. L. W. Exhibits 6 to 12, inclusive.

You may have the witness.

Mr. Gibson: I have only one question.

Cross-examination.

By Mr. Gibson:

Q. I notice in your monthly statements of income for January and February, 1943, being S. L. W. Exhibits 9 and 10, you show income above $82,000 or $83,000, which is roughly the same amount that was shown for the full calendar year of 1942. I wanted to ask you whether this is not true, that the annual statement is after deductions of full contingent interest of $660,000 on the Salt Lake in-

come bonds, whereas no part of such deduction was made in the monthly income statement, is that correct?

A. That is correct.

Q. That explains why the difference?

A. Yes.

Mr. Gibson: Thank you.

. . . . . .

[fol. 1443] Mr. Gibson: If I may say so, I think the record would be improved if I could identify on the record our previous exhibits, which are not now mentioned in the transcript.

Insurance Group Exhibit 1 is the Phipps-Hughes Agreement relating to the purchase of minority stock of the Salt Lake.

Insurance Group Exhibit 2 is the Salt Lake report to stockholders for 1940.

Insurance Group Exhibit 3 is the Salt Lake report to stockholders for 1941.

Insurance Group Exhibit 4 has been reserved for the [fol. 1444] Salt Lake report to stockholders for 1942, and I ask if it may be stipulated that should that document become available before decision by the Court, that it may be admitted in the record.

Mr. Myer: We have no objection.

Mr. McCaffery: On that hypothesis, we do not object.

Mr. Gibson: It is a condition, not a hypothesis.

Insurance Group Exhibit 5 is the Rio Grande report to stockholders for 1940.

Insurance Group Exhibit 6 is the Rio Grande report to stockholders for 1941.

Insurance Group Exhibit 7 has been reserved for the Rio Grande report to stockholders for 1942, and subject to the same condition, I should like to stipulate that it may be admitted when available.

Mr. Myer: We have no objection.

. . . . . .

[fol. 1445] OPINION

The Court: Anyone else want to be heard?

This matter has been pending before the Court, as pointed out in argument, for many years. I see no reason why it should not be decided at this time, rightly or wrongly.

The Salt Lake Western Railroad is certainly entitled to know whether it is going to get any rent for the use of its property. The Court is firmly of the opinion, as it has expressed heretofore, that the Moffat Tunnel, the Dotsero Cut-off and the Salt Lake Railway are public enterprises in which the people of the State of Colorado have a large public interest, especially the taxpayers of the Moffat Tunnel District who have obligated themselves in the sum of over $15,000,000 in bonds to construct this tunnel for the use of these railroads. The public interest in this property is very large, as evidenced by the appearance here of the Moffat Tunnel Commission and also the State of Colorado through the Attorney General.

The agreements here in question were drawn with the idea of effecting a through route from Denver to Salt Lake, and the net result has been to create an additional transcontinental line from the Missouri River to the Pacific Coast. This has been emphasized in the last two years by the tremendous amount of war material and soldiers this route has carried from east to west and vice versa for the Federal Government in the aid of the war effort. The Moffat Tunnel route is now established as a transcontinental route. Were it not for the tunnel this situation would not obtain, and I am one of those who believe that [fol. 1446] as time goes on the use of the tunnel and this short cut line will greatly increase, although I do believe that the Pueblo gateway will always handle more business than the Denver gateway. That has been indicated by what the road has done to date, and I think that will continue. Nevertheless, there will be a large increase of business through both gateways, due to the fact that the Rio Grande railroad and its eastern and western connections at Salt Lake is now established as a transcontinental line.

This whole proceeding is equitable, because, of course, bankruptcy is governed by equitable principles, and for that reason I can see no reason why a bankrupt debtor has the right to take possession of and use the property of a corporation, here the Salt Lake Western Railroad, to the exclusion of everybody else without paying anything for it.

For that reason this rent should be paid in the way I shall hereafter indicate, but before that we have the question of the adoption and approval of these agreements. These have been in existence for a long time. They have

received the approval of the Interstate Commerce Commission and all other bodies, public and private, whenever the question of their necessity or need has been litigated or discussed.

For that reason the order of the Court will be that these agreements in question will be ratified and approved by the Court.

Now, when it comes to the payment of interest, I think the one note, the note that I will designate as the construc-
[fol 1447] tion note, which represents the money lent by the R. F. C. for the construction of the Dotsero Cut-off, stands in a much better position than the other note, which merely represents money borrowed and used by the Rio Grande to acquire the title and capital stock of the Moffat Railroad.

The order therefore will be that the interest on the so-called construction note be paid. As to the stock purchase note, Mr. Myer has frankly admitted his position was not as strong. The Court reserves decision on that question.

On this question of income taxes, the Court is not fully satisfied, and does not feel able at this time to make a decision. I will ask counsel to file briefs in fifteen days on that question relating to the payment of the income tax, whether that shall be paid by the debtor, or by whom, or in what way it shall be handled. You may exchange briefs in fifteen days, and answer each other's briefs in five days thereafter.

Now, in regard to the other question, the Junction bonds, the Court expresses no opinion and has none at this time. The only observation I will make at present is that if anybody wants that matter decided, upon bringing it to the attention of the Court in the usual manner, by giving notice, we will give him an early hearing, and have a complete discussion of it so the Court can decide that question. It seems to me it should be decided. If the people interested therein feel that there have been delays, they are on notice
[fol. 1448] now that they may have the matter determined at any time they want to bring it up on proper notice.

Are there any other questions now that the Court has to pass upon?

Mr. Myer: I suppose I will draw a form of order and submit it to counsel.

The Court: Draw up a form of order, yes.

Mr. Myer: I will have to send it East for approval, so it will be several days.

Mr. McCaffery: If Your Honor please, we have gathered during the discussion here that this may have some effect on the plan, and the Commission no doubt will be much interested in what has taken place here. Would it be in order for me to move Your Honor to instruct the Trustees to send a copy of the transcript to the Commission for its information and consideration?

The Court: You mean the entire transcript?

Mr. McCaffery: Yes, Your Honor.

The Court: It will be pretty expensive, won't it? If you desire, I suppose it can be done.

* * * * * * *

Mr. Gibson: May I ask one other question: If it be Your Honor's decision to direct that a transcript of this hearing be certified or otherwise transmitted to the Interstate Commerce Commission, I wonder if you would not also direct that they be furnished with a transcript of the hearing of May 7, 1936, which was on the same petition of the Salt Lake Trustee, and which was largely relied on by Mr. Myer in this hearing?

[fol. 1449] The Court: That is already in the printed record.

Mr. Gibson: No, that was a transcript of a hearing that was not copied into the printed record. My request, of course, is addressed only in the contingency that it has not been transmitted, or if it has not been it may be.

The Court: Provided the Commission requests it.

Mr. Gibson: If Your Honor please, it was primarily relied on by Mr. Myer as a part of his affirmative case, and we stipulated that this should be a part of the record, to save Your Honor's time and to save the time of counsel. It dealt chiefly with this issue, and the Commission should not have a fragmentary record. If they have anything that was said here, it should be the whole record. I think that is a reasonable request, Your Honor.

The Court: Where is that transcript?

Mr. Myer: I have a copy of it, but I should hate to lose it.

Mr. Gibson: It can be easily reproduced at a very small expense. The issues are large enough to justify the expense.

The Court: All right, it is so ordered.

[fol. 1450] IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO, SITTING AT DENVER

No. 8669

In Proceedings for Reorganization of a Railroad

In the Matter of THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, Debtor

Excerpts from Hearing of September 13, 14 & 15, 1943

HEARING ON OBJECTIONS TO PLAN OF REORGANIZATION AND PETITIONS FOR SERVICES RENDERED AND REIMBURSEMENT OF EXPENSES INCURRED BY COUNSEL AND OTHERS

Be It Remembered that on, to wit, the 13th day of September, A. D. 1943, the same being one of the regular juridical days of the May term, A. D. 1943, this matter came on for hearing before the Honorable J. Foster Symes, Judge of the District Court of the United States for the Judicial District of Colorado.

APPEARANCES:

Messrs. Henry W. Anderson and George D. Gibson of the firm of Hunton, Williams, Anderson, Gay & Moore, and Morrison Shafroth, Esq., of the firm of Grant, Shafroth & Toll, for the Insurance Group.

Messrs. E. R. Campbell and John Q. Dier of the firm of Brock, Akolt & Campbell, as attorneys for Chase National Bank of the City of New York in its capacity as holder of a secured note of debtor, but not as Trustee under Denver and Rio Grande Western Railroad Company Refunding [fol. 1451] and Improvement Mortgage 5s due 1978 and 6s due 1974.

Edward E. Watts, Jr., Esq., of the firm of Mitchell, Capron, Marsh, Angulo & Cooney, and Messrs. Hagnar Holme and Milton J. Keegan of the firm of Dines, Dines & Holme, for City Bank Farmers Trust Company.

Frank H. Heiss, Esq., of the firm of Rathbone, Perry, Kelley & Drye, Max D. Melville, Esq., and Miss Norma L. Comstock for Central Hanover Bank and Trust Company, as Trustee, intervener.

Messrs. Lewis & Grant, and Arthur A. Gammell for Chase National Bank of the City of New York, as Trustee under

The Denver and Rio Grande Western Railroad Company Refunding and Improvement Mortgage dated February 1, 1924, intervener.

William V. Hodges, Esq., of the firm of Hodges, Vidal & Goree, for debtors The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company.

Gail L. Ireland, Esq., Attorney General of the State of Colorado.

Messrs. Lindsey & Larwill for United States Trust Company of New York.

Erskine R. Myer, Esq., for Moffat Tunnel Improvement District, Moffat Tunnel Commission, and H. Allyn Hicks, Esq., Trustee of the debtor The Denver and Salt Lake Western Railroad Company.

H. H. Larimore, Esq., for the Missouri Pacific Railroad Company.

Messrs. W. Meade Fletcher, Jr., and James L. Homire, [fol. 1452] for the Reconstruction Finance Corporation.

Edwin S. S. Sunderland, Esq., and Robert G. Bosworth, Esq., for Guaranty Trust Company of New York, as Trustee and intervener under the Western Consol 4s.

Messrs. J. F. Schneider and William L. Cohn for the Untermyer Family Group.

Messrs. Charles R. Enos and Percival Jackson for George A. Gaston et al.

Henry McAllister, Esq., for the Trustees of The Denver and Rio Grande Western Railroad Company.

W. A. W. Stewart, Esq., for the United States Trust Company of New York.

* * * * * * * *

[fol. 1453] Excerpt from Hearing September 15, 1943

Arthur E. Burke, called and sworn as a witness, on behalf of the debtor, testified as follows:

Direct examination.

By Mr. Hodges:

Q. Will you give your name?

A. Arthur E. Burke.

Q. You are an officer of the Guaranty Trust Company of New York?

A. I am.

Q. Will you state what office you have?

A. Vice President.

Q. Your mortgage has deposited under it the stock of the Utah Fuel Company——

A. That is correct.

Q. —as collateral for the Western Consolidated?

A. Yes.

Q. What we call the Western Consolidated?

A. Yes.

Q. Will you give the appropriate title of that mortgage?

A. The Rio Grande Western Consolidated Mortgage, due 1944.

Q. And that stock is in your possession?

A. It is.

Q. Has the Guaranty Company been watchful of the operations of that coal company since this reorganization proceeding was initiated?

A. They have.

Q. Now, what is the character of the reports of that operation which you have received?

Mr. Sunderland: May I interrupt before the witness [fol. 1454] answers? If Your Honor please, I object to this line of inquiry. In the first place, the Supreme Court has held, as I view their decisions, that evidence dealing with the period up to the closing of the case before the Commission, may not be inquired into in a hearing of this kind, which is a hearing on the Commission's approved plan. Any evidence that has to do with any exceptional circumstance or event following the closing of the case, in our view of the holding of the Supreme Court, may be considered by Your Honor, but to go over the evidence that is before the Commission, on which it based its decision, at this time, as a matter of review, or going into the question of anything before the Commission, is entirely irrelevant and immaterial, and I object to this line of inquiry.

The Court: What is your authority?—the Milwaukee case?

Mr. Sunderland: Yes.

The Court: Will you point out the language you have in mind?

Mr. Sunderland: With reference, now, to the Supreme Court decision in Group of Investors vs. Milwaukee, it says:

"As we have indicated in the Western Pacific case, the power of the District Court to receive additional evidence may aid it in determining whether changed circumstances require that the plan be referred back to the Commission for consideration."

The Court: What page is that?

Mr. Sunderland: It is in 318 U. S., at Page 542, about the middle of the page. "The question put to the witness [fol. 1455] deals with the earnings of the Utah Fuel for the period covered by the evidence before the Commission, and it has nothing to do with any changed circumstance with respect to the record made before the Commission.

The Court: Read the question.

(Last question read.)

The Court: Wasn't that before the Commission?

Mr. Hodges: No, Your Honor. In the first place, the Commission had nothing whatever to do with fixing the amount of the claim as proved in this court. It has absolutely nothing to do with it. That is part of the job of this Court. So that the language of the Supreme Court has only to do with those findings that the Commission has something to do with. In the second place, this is a preliminary question, and I will ask him if he got the reports, when we come to the reports, and then we will see if I am asking him about anything that anybody testified to before the Commission.

The Court: He may answer. I will reserve decision.

The Witness: Will you read the question?

(Last question read.)

A. Well, we received periodical reports. We received, of course, annual reports, and I believe we received quarterly reports.

Q. Now, what do they cover?

A. Well, they cover the usual things a report of that character would cover—the earnings, the asset position—the usual financial reports of the company.

Q. Do they cover the operating details?

[fol. 1456] A. Yes, of that company.

Q. The amount of coal sold?

A. The amount of coal sold.

Q. The amount received for it?

A. Yes, I believe so.

Q. The expenses incurred in mining?

A. Yes, I believe they do.

Q. And transportation, and all the other items that would be chargeable against the amount received, in order to determine the amount earned; is that correct?

A. Well, I don't know. It might be. I haven't the reports here, and I haven't looked at them within a reasonably short time, as to each item of transportation, and so forth.

Q. I am not asking you for the items.

A. I know, but you put the words in my mouth.

Q. Well, what I wanted to ask you was, a full characterization of reports.

A. All I can say is that we have received statements, yes, as to the operations, the number of tons of coal, the cost, and other items, but as to those items, I couldn't say offhand, such as transportation.

Q. You were asked the other day if you had any of those reports here.

A. I was asked by you, and I said I did not bring them along.

Q. And it is true that you have none of those reports here?

A. I brought no reports along whatsoever.

Q. I am referring to the reports of the Utah Fuel Company. That is what I am speaking of.

A. Yes.

Q. Have you any memorandum made up by you from those reports with you?

A. I have not. I did not anticipate I would go on the stand and be asked any questions about it, or to give any evidence.

[fol. 1457] Q. Was there reported to you any information as to the growth, if any, of the market for the coal from that property?

A. You mean over a short period? I don't know as I understand your question.

Q. Well, I take it that that could be answered as to a long or a short period.

Mr. Sunderland: If Your Honor please, I request that the period be indicated.

Mr. Hodges: I will indicate the period when I find out that he really is going to be helpful or whether he is not.

If he is going to be helpful, I will ask him to the extent to which he can be helpful.

Q. Has any information been given to you respecting long-term contracts for the output of that property?

A. Will you define "long-term"? I know there have been contracts signed, but as to their duration I am not certain.

Q. Within what limits is that uncertainty? Would you say, with assurance, that they would run for two years?

A. I believe so.

Q. Would you say, with assurance, that they would run for ten years?

A. No, I could not.

Q. Well, as between those two extremes, where is the period of time when you would become hazy as to your knowledge of the length of service entered?

A. Right from the very start, because I am not certain whether those contracts, frankly, were for one year, or two years, or ten years. I know there were certain contracts entered from time to time, but as to their duration I am just not at all certain now.

[fol. 1458] Q. Of course, what I should like to know from you is, first, what the profits of that operatio. have been since the date that the last testimony was taken before the Interstate Commerce Commission. Now, I will get that date for you. It should be in this record, but it is not. It will take me some little time to get that date.

A. Well, the date would not help very much, Mr. Hodges, because I do not know what those earnings are, offhand. As I said before, I did not come prepared to testify on anything on the Utah.

Q. I understand, but I would like to get this date.

The Court: Can anybody find that date?

Mr. Anderson: I am sure it was early in 1941.

Mr. Gibson: May 20, 1941.

Mr. Hodges: May 20, 1941. We will insert that date, and then have the question read. Will you read it?

(Pending question read as follows: "What I would like to know from you is, first, what the profits of that operation have been since the date that the last testimony was taken before the Interstate Commerce Commission, May 20, 1941.")

Mr. Hodges: I think he answered that. Will you read the answer?

(Last answer read.)

Q. Now, it is perfectly possible, Mr. Burke, for you to say that you do not know what those earnings were, and at the same time you have in your mind an approximate figure; is that true?

A. No, not altogether. I have seen the earnings, yes, [fol. 1459] going back approximately two years for the date, and I have seen the earnings for 1941, and I have seen the earnings for 1942, and possibly for this year, but as to the exact amount of those earnings, or even the approximate amount of earnings, with war taxes and other taxes, I just would not want to say; it would be pure guesswork; I might be way off.

Q. Now, in your watchfulness over the security that is behind the bonds of your bondholders, you haven't fixed in your mind any figure approximating the income from this Utah Fuel stock; is that correct?

A. No, it is not correct.

Q. Then you have a figure approximating the income of the Utah Fuel stock?

A. Well, any figure I have in my mind I do not think is fair to give, because I don't know whether that figure is correct.

Q. When you speak about "correct," you mean you cannot say that it would be an audited figure; is that so?

A. I mean I am not absolutely certain what those figures are. As I say, I have not looked at them for the purpose of testimony, which I did not expect to give. I see a good many figures every day, and a good many things.

Q. I can understand that. Yesterday I referred to a telegram which refers to a report of the Utah Fuel Company for the year 1942, showing net surplus for the year of $415,000. Does that figure correspond fairly closely with your recollection of what it was for that year?

A. Yes, it does.

Q. And in the period from January 1 to July 31, 1943, the surplus was $535,869. That is the half-year of 1943. [fol. 1460] A. Do you mean the earnings—the surplus of earnings?

Q. Yes.

A. That sounds possibly correct.

Q. You have had, I take it, no figure showing an estimate for the total earnings of 1943?

A. I don't think so. I have seen some earnings, but as to whether that was projected through the balance of 1943, I don't believe it was, with the question of income taxes coming in there.

Q. That was the figure of $877,609, as representing the earnings for the year—estimated earnings for the year 1943?

A. Well, as I say, I don't recall any estimate for the balance of 1943.

Mr. Hodges: I think that is all.

The Court: Is there any cross-examination? That is all, Mr. Burke.

(Witness excused.)

Mr. Hodges: I would like to make a statement of facts that I do not think anyone would dispute. I had sent for Mr. Thompson, but he is not here. The Court's Trustees have not considered that this Utah Fuel stock was at all in their care, and have not kept the Utah Fuel accounts. That is my information.

The Court: Is that correct, Mr. McCarthy?

Mr. Hodges: And the Fuel Trustees have not considered the Utah Fuel stock as a part of your trust, and have not kept accounts on it.

Mr. McCarthy: Well, I do not know what accounts were kept by the Utah Fuel. I take it that Mr. Thompson might have made the reports. I do not know what Mr. McAllister required, nor what examination had been made. Surely [fol. 1461] we should not be prosecuted for having some interest in the Utah Fuel Company; at least, I am convinced that the ownership was so remote and contingent that we at least should not be indicted; and not long ago—I don't know whether you want this in the record or not—the matter was again brought to my attention, and intimated that there was still a possibility of something like that occurring. So that inasmuch as it was contended that we had an ownership in this stock, a remote ownership which was contrary to the Elkins Act, that therefore we should stay just as far away from it as possible.

That is about all I know about it.

Mr. McAllister: I can confirm what Judge McCarthy says, and from that time there was nothing kept in the Rio Grande books about the Utah Fuel.

[fol. 1462] OPINION

The Court: Is that all, gentlemen? Anybody else have anything more? Apparently the time has come in this proceeding when the Court is required to pass upon this plan. It it not the first one that has been proposed in this matter, as you all know. The debtor and the parties themselves have proposed plans which were rejected by the ICC, and the Court of its own motion submitted a plan which it felt really met the situation at the time, but that was for good reasons, undoubtedly, rejected by the Commission.

It seems to me in passing upon this plan the Court should take into consideration the fact that this litigation should sometime be terminated and brought to an end, and the property returned to the people who own it. The federal courts are not equipped to permanently run a railroad, any more than they are any other enterprise. However, the Court feels, and I think all the parties should realize, that the property has been well managed during the period that it has been in the court. This is due, of course, to the splendid service performed by the two Trustees, Mr. McCarthy and Mr. Swan, to whom too much praise cannot be given for the present condition of the property. When they took it over it was a wreck. There were great lengths of track or main line where trains could not be operated except under slow orders. The equipment was broken down and there was a great deal of legitimate and proper complaint from the customers of the road as to the service given. As you all know, during this trusteeship the road has been completely rehabilitated, and today is doing a splendid job as one of the main transcontinental lines of [fol. 1463] this country. If this had not been done there would have been a serious shortage in transportation available for the war effort from the Pacific Coast to the Eastern Coast, which would have seriously interfered with the war effort.

This is the fourth time this road has been in receivership, the second time since I have been on the bench. The last proceeding was an equity proceeding before Section 77 was enacted, and the plan drawn by the securityholders, which came out of that proceeding, proved entirely inadequate to the situation, principally, I think, because of the high capitalization that the plan provided for, and, secondly, because between that receivership and this one the road was not properly managed, the interest of the public was not considered, and the road was not properly maintained.

The road now goes back to the owners in the same condition it did then—splendid condition, good roadbed, good equipment, and with a personnel and organization and working force that is second to none in this country in their loyalty to the property, and their desire to serve the public, and I may express the hope that splendid spirit which now prevails in this organization will not be destroyed by the new management when they take over.

I have often made the observation that in bankruptcy matters those who come into the bankruptcy court as creditors do not realize that they must take a loss on their securities, whatever they may be. This railroad could not come into this court under bankruptcy had it not been that the creditors had already sustained a loss which they must [fol. 1464] take and which must be reflected in any sound plan of reorganization. There seems to be a belief among people that the bankruptcy court by some legerdemain or magic can restore values when they do not exist and restore values that have been wiped out by mismanagement. Creditors must assume their loss and blame themselves for a poor investment, and not blame it upon the court.

The Supreme Court has clearly indicated our duty in two recent cases, i. e., the Western Pacific and the Milwaukee, and given a clear interpretation of this act, the constitutionality of which has been upheld by the Supreme Court.

Some of counsel have urged that the Court should overrule and substitute its judgment for that of the ICC in matters which those decisions indicate the Court cannot interfere with, and on which the findings of the Commission are binding upon the Court. It is our duty to do that, and we shall attempt to comply to the best of our ability.

The Court feels that this plan is feasible, and that it meets all the requirements of Section 77 preliminary to

approval of the plan by the Court. Those are that the Court must be and is satisfied that it complies with the provisions of subsection (b) of Section 77, that it is fair and equitable, affords due recognition to each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and conforms to the requirements of the law of the land regarding the participation of the various classes of creditors and [fol. 1465] stockholders; that the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of this hearing, and that they are reasonable and within the maximum limits as fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; further, that the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except the allowances provided for in subsection (c), paragraph (12) of this section, which may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

So, gentlemen, in conclusion let me say that I overrule all objections and approve this plan. The steps necessary to carry it out as required by the statute may be taken.

* * * * * * *

[fol. 1466] [Stamp:] United States District Court, Denver, Colorado. Filed Jan. 2, 1945. G. Walter Bowman, Clerk

IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO, SITTING AT DENVER

No. 8669

In the Matter of the DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, Debtor

In Proceedings for the Reorganization of a Railroad

Before Honorable J. Foster Symes

Denver, Colorado, November 15, 1944.

APPEARANCES:

Thomas R. Woodrow, Esq., for The Denver and Rio Grande Western Railroad Company.

Morrison Shafroth, Esq., for the Insurance Group.

Erskine R. Myer, Esq., for H. A. Hicks, Jr., Trustee of The Denver and Salt Lake Western Railroad Company.

[fol. 1467] HENRY SWAN, called as a witness, being first duly sworn, testified as follows:

Direct examination.

By Mr. Woodrow:

Q. State your name, please.

A. Henry Swan.

Q. You are one of the Trustees of the Debtor Railroad Company?

A. Yes, sir.

Q. You are familiar in a general way with Schedule 26 which is attached to the Petition now before the Court, are you not, Mr. Swan?

A. Yes, sir.

Q. And the Trustees have approved all of these expenditures which are asked for in the Petition?

A. Yes, sir.

Q. Study has been given as to the ability of the Railroad to take care of the cash required in making these expenditures, I assume; is that true?

A. Yes, sir.

Q. And is it your opinion that the cash resources of the Railroad at the present time, with the probably income obtained in 1945, will enable you to make these expenditures without in any manner avoiding any necessity of taking care of the Trustees' obligations or the Railroad's obligations under the proposed reorganization plan?

A. The resources are ample.

Mr. Woodrow: Do you want to cross-examine?

[fol. 1468] Cross-examination.

By Mr. Shafroth:

Q. Mr. Swan, have you made a comparison of the net earnings of the years 1933 and 1934 with the requirements of the plan for those years?

A. 1943 and 1944?

Q. Yes, I beg your pardon, 1943 and 1944.

A. In each of the years 1943 and 1944 certain charges will accrue under the plan by reason of the earnings of the Railroad for those two years.

Q. Can you tell me what the net earnings for 1943 and 1944 are?

A. I can't give you the net earnings for 1944 yet, but the net earnings for 1943 were about $11,000,000 available for interest.

Q. $11,573,667.94, is that correct?

A. Yes, it shows in the annual report.

Q. Have you an estimate for 1944 of the earnings?

A. I haven't up to December first, but they are large enough for the accruing charges provided for under the plan.

Q. What I am trying to get at, Mr. Swan, is whether or not the expenditures proposed in this budget can be taken care of out of the earnings for the years 1943, 1944, and 1945, which would be available for dividends on the common stock; in other words, whether or not the requirements of the pian can be fully taken care of, including the accumulative preferred dividend, and leave a sufficient surplus out of earnings to take care of this proposed expenditure.

A. This proposed expenditure can be taken care of out of the funds that are available from earnings for 1943 and 1944, plus what we expect to accumulate in 1945, without impairing in any way the accruals under the plan through [fol. 1469] the preferred stock dividends, but not including any dividends on the common stock.

Q. No, of course, not. In other words, as I understand it, the earnings for 1943 and 1944, with a reasonable anticipation, without attempting to estimate the 1945 earnings, but with a reasonable anticipation of some earnings in 1945, will be sufficient to take care of all of the requirements of the plan, and leave sufficient to take care of this budget.

A. That is correct.

Q. Do you suppose it would be too much trouble to get Mr. Thompson to make up a little exhibit making that comparison?

A. I have in my hand a statement which we have prepared in order to reply to a telegram which comes to us from Mr. Gibson, who asked the same question that Colonel Anderson has asked you to ask me. It shows, without reference to the capital fund provided in the plan that for the year 1943 the accruals under the plan will be as follows: First Mortgage, fixed 3%, $1,679,225; Prior Contingent 1%, $559,742; Sinking Fund 1st, $171,703; Income Bonds 4½%, $944,057; Sinking Fund Incomes, $56,941; 5% Preferred Stock, $1,859,810. Now, that is the base accrual of each succeeding year, with one exception. That is as our Equipment Trust charges develop they should be added to that.

Q. The figures you gave are for 1943?

A. That is correct. Precisely the same figures appear for 1944, because we have already paid off obligations due this year. Next year we will have $609,000 Equipment Trust due, and $110,284 interest, so that while this year and last year I did not add this into the charge against the earnings, nevertheless next year we will have to provide for that out of cash, not as a charge against earnings, [fol. 1470] except so far as interest is concerned.

Now, then we have paid under Court Order 534 $2,398,679. The balance that has not been paid but accrued in 1943 is $2,872,799, and the total accruals for 1944, $5,271,478, and the accruals both for 1943 and 1944, $8,144,277. Now, in 1945 the amount of——

Q. Before you get to 1945, are the 1944 earnings running approximately the same as the 1943 earnings, or in excess of them?

A. I haven't the detail in my mind.

Q. Even approximately? You couldn't even give it to me approximately?

A. Well, I can telephone and get it exactly for you, get the earnings. (The following information was supplied by the witness at the close of his testimony: Balance available for interest, dividends, etc., up to September 1, 1944, $8,506,004.)

Now, we have to take into account our cash reserves in figuring not only the accruals but also these contemplated expenditures. Contemplated expenditures for this schedule, as well as contemplated expenditures for uncompleted items of previous schedules, and also for the payment of income taxes covering earnings for the year 1944, payable in 1945, and also for the deferred maintenance for which reserves have been set up. Our cash situation is as follows: Estimated balance January 1, 1945,—now, these figures will appear on this sheet—$5,487,000; Government Securities, $13,500,000; Tax Notes, $3,005,000;——

Q. 500,000 or 5000?

A. 5000. Cash in Deferred Maintenance Fund, which is a special separate earmarked fund, $304,000, or a total cash reserve on January first of $22,296,000. Appropriations and commitments against that fund are as follows: [fol. 1471] Reserve for Deferred Maintenance, $3,304,000; this current improvement program and the carryover from the previous programs, $7,000,000; Income Tax estimated against the earnings for 1944, payable in 1945, $5,000,000; a total of $15,304,000, or a balance available for the charges which have accrued under the plan of $6,992,000. These charges, however, up to December 31 of this year aggregate $8,144,277, so there will be a deficit, without giving any consideration to the earnings of 1945, of $1,152,277.

Q. It is not unreasonable to assume that that deficit will be more than earned in 1945?

A. It is very definite this sum will be obtained from the operations of the property in 1945, without any deficit. Now, you can take this, (presenting paper).

Mr. Shafroth: If you will just file that paper as an exhibit, I think it covers everything, Mr. Swan. I think that is all.

(Discussion off the record.)

Mr. Woodrow: I have no further testimony.

(Argument.)

Mr. Woodrow: I desire to submit an order approving and authorizing the expenditures.

The Court: You may have the order. It will be signed.

[fol. 1472] In United States District Court

Hearing of November 20, 1944

(Clerk's Note:) In open court, on November 20, 1944, Mr. William V. Hodges, on behalf of the Debtor and the Denver and Salt Lake Railroad Company, made the following motion:

"I move the Court to determine or send to a Master for determination and report the amounts due each class of creditors and for which each class is entitled to recognition in the distribution of securities in any plan of reorganization; the allocation of earnings to the various classes of creditors during the period of administration, the necessary credits from earnings, by how much, if any, the debtor's assets are inadequate to pay debtor's obligations as of November 15, 1935, and if debtor's assets are more than adequate to pay the said claims as they existed on that date, what equitable claims have the creditors, or either of them, to such excess of assets, and by what equitable right is the debtor's interest in them forfeited or denied to it.

"Debtor records its claim that the questions of fact and law suggested in this motion are for determination within the jurisdiction of the Court and not within the powers or jurisdiction of the Commission to determine."

[fol. 1473] IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO, SITTING AT DENVER

No. 8669

In Proceedings for Reorganization of a Railroad

In the Matter of the DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, Debtor

HEARING ON ORDER FOR CONFIRMATION OF PLAN AND MOTION OF WILLIAM V. HODGES

Be It Remembered that on, to wit, the 29th day of November, A. D. 1944, the same being one of the regular juridical days of the May Term, A. D. 1944, of said court, this cause came on for hearing before the Honorable J. Foster Symes, Judge of the District Court of the United States for the Judicial District of Colorado.

APPEARANCES:

Henry McAllister, Esq., for the Trustees of the debtor, The Denver and Rio Grande Western Railroad Company.

William V. Hodges, Esq., of the firm of Hodges, Vidal & Goree, for the debtors The Denver and Rio Grande Railroad Company and the Denver and Salt Lake Railroad Company.

Morrison Shafroth, Esq., of the firm of Grant, Shafroth & Toll, for the Insurance Group Committee.

Milton J. Keegan, Esq., of the firm of Dines, Dines & Holme, for City Bank Farmers Trust Company, as Trustee.

Robert G. Bosworth, Esq., of the firm of Pershing, Bosworth, Dick & Dawson, for the Guaranty Trust Company of New York, as Trustee.

[fol. 1474] Thereupon the following proceedings were had:

The Court: Denver and Rio Grande Western Railroad Company hearing on the order to confirm. Mr. Hodges.

Mr. Hodges: May it please the Court, when this matter came up for hearing on the entry of an order to confirm the plan I made a motion which your Honor set for hearing this morning. The motion is on the record, dictated on the record.

The Court: I thought you had a written piece of paper.

Mr. Hodges: I did, and that was at your suggestion read into the record, and the reporter put it in the record and has furnished copies to the parties. That motion, to refresh your recollection, is a motion to have the Court determine or send to a master for determination for the Court the amounts due each class of creditors and for which each class is entitled to recognition in the distribution of securities in any plan of reorganization; second, the allocation of earnings to the various classes of creditors during the period of administration, the necessary credits from earnings, by how much, if any, the debtor's assets are inadequate to pay debtor's obligations as of November 15, 1935, and if debtor's assets are more than adequate to pay the said claims as they existed on that date, what equitable claims have the creditors, or either of them, to such excess of assets, and by what equitable right is the debtor's interest in them forfeited or denied to it.

Debtor records its claim that the questions of fact and law suggested in this motion are for determination within the jurisdiction of the Court and not within the powers of [fol. 1475] jurisdiction of the Commission to determine.

(Thereupon argument was had on the motion by Mr. Hodges, Mr. Shafroth and Mr. Bosworth.)

The Court: Do you care to be heard?

Mr. Keegan: Do I understand what we are discussing now is limited to the motion? We have here this morning this order that was submitted by Mr. Gibson, confirming the plan, and also I understand from Mr. Shafroth he is submitting another order regarding the petition of the City Bank Farmers Trust Company for construction of the plan. I do have a statement to make on those two proposed orders. I just simply want to state that the City Bank Farmers Trust Company, as Trustee under the General Mortgage, objects to the substance of these orders that have been submitted, the order prepared by Mr. Gibson, confirming the plan, and also the one Mr. Shafroth has, denying the petition of the City Bank Farmers Trust Company. That is all the statement I care to make at this time, your Honor.

Thereupon a recess was taken until one thirty o'clock p.m.

Pursuant to recess the following proceedings were had at one thirty o'clock p.m.:

The Court: Did you finish, Mr. Keegan?

Mr. Keegan: Yes. I think that our position was so thoroughly covered in the arguments and in the hearing on the confirmation of the plan that I see no point in my [fol. 1476] making any additional argument at this time.

The Court: All right.

(Thereupon further argument was had by Mr. Hodges.)

OPINION

The Court (from the bench): Mr. Hodges by his motion wants this proceeding held up pending a hearing to determine what is due each class of creditors and what each is entitled to in the distribution of new securities in any plan of reorganization. When we consider the procedure prescribed by the statute, Section 77, and what proceedings have been had in this case, that is just what has been done. The Commission has valued the property. They have fixed the amount of the claims of the different mortgages, ranked them in order of their priority, and, pursuant to the decisions of the Supreme Court, have allowed interest thereon up to the effective date of the plan. I cannot see anything inequitable in the allowance of interest. I have always felt that a creditor was as much entitled to his interest in reorganization as he is to his principal. When people can buy securities, they are more interested by the rate of interest to be paid than they are in their principal. They contract for both, and we cannot see why they should be deprived of their interest any more than they can have the amount of their principal cut down, which is only done when the value of the property is not sufficient to meet the principal due after all claims are marshalled. This matter is one to which the Commission has devoted a great deal of time, and one with which this Court under the decisions of the Supreme Court has nothing to do.

[fol. 1477] Something has been said about equitable principles. The whole theory of bankruptcy and the whole bankruptcy structure in the Federal courts is based upon equitable principles, and I think they are fully applied in this reorganization act. Everybody has had a right to a hearing. The statute is based upon equitable principles and the right of everybody to be heard.

A plan of reorganization must meet certain requirements, as has been here well said. It grants the Commission and the Court in the course of the proceeding power to change the rights of the parties. All previous rights of the debtor are really wiped out. It creates new securities. The old creditors secure new rights and the same property is back of their new securities as was back of the old securities, so they do not lose anything. But the basic principle that is too often overlooked in these Section 77 cases is that, as emphasized in the Milwaukee and Western Pacific cases, the Commission plan "(4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof." Applying this language to this railroad, it has over a course of years demonstrated it can earn a certain amount, and this proviso requires that those earnings be capitalized in such an amount as the history of the property demonstrates can be earned, and if the previous capitalization was so large, as was the case [fol. 1478] of this railroad, that it cannot earn the fixed interest on the old capital structure, that capital structure must be wiped out and a new one set up which there is some probability that the property can carry.

A great deal has been said about the swollen or large earnings of this property for the last three or four years, but, as I have pointed out several times and the Supreme Court has said in allied cases, wartime earnings are no criterion for capitalization of what a property will earn over a period of years. In other words, just because when these new securities are issued earnings are away up, as they are today, they form no basis for the belief that over the life of these securities such earnings will continue. In fact, the history of this property is such that it is very doubtful in my mind if the new capital structure is not too large and the fixed charges are not too great. Had that been in my sole province to decide, I might have—I don't say I would have—provided for lower fixed charges, which would necessarily cut down the amount of new securities to be issued.

All the questions argued and urged by Mr. Hodges have been answered by the Supreme Court in construing this act since the beginning of its operation. It has been held constitutional by the Supreme Court in several cases and its meaning very clearly stated. The parts the Court and the Commission shall play in the reorganization of property have been clearly delimited by that Court. We must, of course, stay within those rulings. A good deal I have been and am asked to do in rejecting this plan and applying so-called equitable principles runs counter to the decisions [fol. 1479] of the Courts of Appeals, which I must recognize.

So I do not see anything to do but to confirm the plan and deny this motion. Likewise I shall make an order formally denying the petition of the City Bank Farmers Trust Company which I have already discussed in a memorandum on confirmation.

For these reasons the motion of Mr. Hodges will be overruled and exceptions allowed; and the plan formally confirmed.

Is there any discussion about this suggested order? Who has agreed to this?

Mr. Shafroth: That has been submitted to everybody I believe, your Honor, and all of the Trustees, that is, the Reconstruction Finance Corporation, the Insurance Group and the Trustees, and while Mr. Keegan's client has not agreed to the substance of it, I think as to form they have made no objection, and I think the same is true of Mr. Hodges.

Mr. Hodges: We do not object to the form. We object to the substance.

The Court: That being the case, on the statement of counsel that it has been approved by all interested parties, with few exceptions, I will sign this order as submitted.

Mr. Keegan: If the Court please, I understand that the objections and exceptions of the City Bank Farmers Trust Company, as Trustee under the General Mortgage, will be shown in the record to these orders.

The Court: Will you file them?

Mr. Keegan: I would like to now object and state just for the record——

(Here follow 2 photolithographs, side folios 1480, 1481)

Exhibit ___

Witness A

THE DENVER AND RIO GRANDE WESTERN SYSTEM

PROPOSED PLAN OF CONSOLIDATION AND REORGANIZATION AS OF JANUARY 1, 1937

FINANCE DOCKET NO. 11002

Consolidated Balance Sheet - December 31, 1935

Columns	Denver and Rio Grande Western Railroad Co. (1)	Rio Grande Junction Ry.Co. (2)	Denver & Salt Lake Western R.R. Co. (3)	Goshen Valley RR Co. (4)	Denver & Salt Lake Ry.Co. (5)	Inter Company Eliminations (6)	Total All Companies (7)	Pro Forma Balance Sheet (8)
ASSETS								
Investments:								
Investment in Road and Equipment	$210,625,971	$5,228,792	$3,645,460	$503,941	$16,306,104		$236,310,268	$225,408,728
Improvements on Leased Railway Property	403,887				404,571		808,458	808,458
Deposits in Lieu of Mortgaged Property Sold	37,875						37,875	-
Miscellaneous Physical Property	155,032						155,032	155,032
Investments in Affiliated Companies	15,523,611				29,666	$14,936,258	617,019	617,019
Other Investments	34	900			820,925		821,859	821,859
Total Investments	$226,746,410	$5,229,692	$3,645,460	$503,941	$17,561,266	$14,936,258	$238,750,511	$227,811,096
Current Assets:								
Cash	$ 1,153,055	$ 764	$ 571		$ 142,351		$ 1,296,741	$ 1,412,771
Special Deposits	112,296	2,050	61		1,977,725		2,092,132	2,013,977
Loans and Bills Receivable	81,240		3,110,850			3,110,850	81,240	81,240
Traffic and Car Service Balances Receivable	188,416				155,125	11,573	331,968	331,968
Net Balances Receivable from Agents & Cond'rs.	78,935				10,646		89,581	89,581
Miscellaneous Accounts Receivable	1,712,981		145,476		136,739	737,001	1,258,195	1,258,195
Material and Supplies	2,600,882				352,132		2,953,014	2,953,014
Interest and Dividends Receivable					6,411		6,411	6,411
Rents Receivable	33,141	58,333			32,473	90,806	33,141	33,141
Other Current Assets	5,721				369		6,090	6,090
Total Current Assets	$ 5,966,667	$ 61,147	$3,256,958		$ 2,813,971	$ 3,950,230	$ 8,148,513	$ 8,186,388
Deferred Assets:								
Working Fund Advances	$ 8,464				$ 105		$ 8,569	$ 8,569
Other Deferred Assets	161,408				28,038		189,446	189,446
Total Deferred Assets	$ 169,872				$ 28,143		$ 198,015	$ 198,015
Unadjusted Debits:								
Rents and Insurance Premiums Paid in Advance	$ 3,190				$ 8,198		$ 11,388	$ 11,388
Other Unadjusted Debits	10,313,744	$ 50,000			93,786	$ 9,422,364	1,035,166	984,866
Total Unadjusted Debits	$ 10,316,934	$ 50,000			$ 101,984	$ 9,422,364	$ 1,046,554	$ 996,254
Total Assets	$243,199,883	$5,340,839	$6,902,418	$503,941	$20,505,364	$28,308,852	$248,143,593	$237,191,753
LIABILITIES								
Capital Liabilities:								
Stock:								
Capital Stock:								
Common	$ 62,457,540	$2,000,000	$3,631,000	$ 50,000	$ 5,393,082	$11,074,082	$ 62,457,540	$ 200,000
Preferred	16,445,600						16,445,600	33,621,940
Funded Debt Unmatured	120,541,000	2,906,000			13,500,000	2,172,000	134,775,000	83,954,849
Grants in Aid of Construction	800,313						800,313	800,313
Nonnegotiable Debt to Affiliated Companies		278,951	14,460	453,941		747,352		
Total Capital Liabilities	$200,244,453	$5,184,951	$3,645,460	$503,941	$18,893,082	$13,993,434	$214,478,453	$118,577,122
Current Liabilities:								
Loans and Bills Payable	$ 6,964,589		$3,110,850			$ 3,110,850	$ 6,964,589	$ 35,000
Traffic and Car Service Balances Payable	501,801				$ 25,838	11,573	516,066	516,066
Audited Accounts and Wages Payable	6,876,763	$ 50,000	73,850		199,188	5,753,852	1,445,949	1,395,646
Miscellaneous Accounts Payable	16,946				23,345		40,291	40,292
Interest Matured Unpaid	7,294,005	52,050	61,690		101,725		7,509,470	380,495
Funded Debt Matured Unpaid	2,003,000						2,003,000	3,000
Unmatured Interest Accrued	1,220,813	8,333	10,568		$660,000	22,258	1,827,456	49,559

Exhibit 25 1066A

Witness Am. Hyer

ompany tions	Total All Companies	Pro Forma Balance Sheet	
	(7)	(8)	
	$236,310,268	$225,408,728	
	808,458	808,458	
	37,875	-	
	155,032	155,032	
56,258	617,019	617,019	
	821,859	821,859	
56,258	$238,750,511	$227,811,096	
	$ 1,296,741	$ 1,412,771	
	2,092,132	2,013,977	
10,850	81,240	81,240	
11,573	331,968	331,968	
	89,581	89,581	
37,001	1,258,195	1,258,195	
	2,953,014	2,953,014	
	6,411	6,411	
90,806	33,141	33,141	
	6,090	6,090	
50,230	$ 8,148,513	$ 8,186,388	
	$ 8,569	$ 8,569	
	189,446	189,446	
	$ 198,015	$ 198,015	
	$ 11,388	$ 11,388	
22,364	1,035,166	984,866	
22,364	$ 1,046,554	$ 996,254	
08,852	$248,143,593	$237,191,753	
74,082	$ 62,457,540	$ 200,000	
	16,445,600	33,621,940	
72,000	134,775,000	83,954,849	
	800,313	800,313	
47,352			
93,434	$214,478,453	$118,577,122	
10,850	$ 6,964,589	$ 35,000	
11,573	516,066	516,066	
53,852	1,445,949	1,395,648	
	40,291	40,292	
	7,509,470	380,495	

Loans and Bills Receivable	81,240		3,110,850			3,110,850	81,240	6
Traffic and Car Service Balances Receivable	188,416				155,125	11,573	331,968	33
Net Balances Receivable from Agents & Cond'rs.	78,935				10,646		89,581	8
Miscellaneous Accounts Receivable	1,712,981		145,476		136,739	737,001	1,258,195	1,25
Material and Supplies	2,600,882				352,132		2,953,014	2,95
Interest and Dividends Receivable					6,411		6,411	
Rents Receivable	33,141	58,333			32,473	90,806	33,141	3
Other Current Assets	5,721				369		6,090	
Total Current Assets	$ 5,966,667	$ 61,147	$3,256,958		$ 2,813,971	$ 3,950,230	$ 8,148,513	$ 8,18
Deferred Assets:								
Working Fund Advances	$ 8,464				$ 105		$ 8,569	$
Other Deferred Assets	161,408				28,038		189,446	18
Total Deferred Assets	$ 169,872				$ 28,143		$ 198,015	$ 19
Unadjusted Debits:								
Rents and Insurance Premiums Paid in Advance	$ 3,190				$ 8,198		$ 11,388	$ 1
Other Unadjusted Debits	10,313,744	$ 50,000			93,786	$ 9,422,364	1,035,166	98
Total Unadjusted Debits	$ 10,316,934	$ 50,000			$ 101,984	$ 9,422,364	$ 1,046,554	$ 99
Total Assets	$243,199,883	$5,340,839	$6,902,418	$503,941	$20,505,364	$28,308,852	$248,143,593	$237,19
LIABILITIES								
Capital Liabilities:								
Stock:								
Capital Stock:								
Common	$ 62,457,540	$2,000,000	$3,631,000	$ 50,000	$ 5,393,082	$11,074,082	$ 62,457,540	$ 20
Preferred	16,445,600						16,445,600	33,62
Funded Debt Unmatured	120,541,000	2,906,000			13,500,000	2,172,000	134,775,000	83,95
Grants in Aid of Construction	800,313						800,313	80
Nonnegotiable Debt to Affiliated Companies		278,951	14,460	453,941		747,352		
Total Capital Liabilities	$200,244,453	$5,184,951	$3,645,460	$503,941	$18,893,082	$13,993,434	$214,478,453	$118,57
Current Liabilities:								
Loans and Bills Payable	$ 6,964,589		$3,110,850			$ 3,110,850	$ 6,964,589	$ 3
Traffic and Car Service Balances Payable	501,801				$ 25,838	11,573	516,066	51
Audited Accounts and Wages Payable	6,876,763	$ 50,000	73,850		199,188	5,753,852	1,445,949	1,39
Miscellaneous Accounts Payable	16,946				23,345		40,291	4
Interest Matured Unpaid	7,294,005	52,050	61,690		101,725		7,509,470	38
Funded Debt Matured Unpaid	2,003,000						2,003,000	
Unmatured Interest Accrued	1,220,813	8,333	10,568		*660,000	72,258	1,827,456	4
Unmatured Rents Accrued	93,912					40,806	53,106	5
Other Current Liabilities	19,073				3,475		22,548	
Total Current Liabilities	$ 24,990,902	$ 110,383	$3,256,958		$ 1,013,571	$ 8,989,339	$ 20,382,475	$ 2,49
Deferred Liabilities:								
Other Deferred Liabilities	$ 369,572	$ 315			$ 13,638		$ 383,525	$ 38
Total Deferred Liabilities	$ 369,572	$ 315			$ 13,638		$ 383,525	$ 38
Unadjusted Credits:								
Tax Liability	$ 1,106,788				$ 177,326		$ 1,284,114	$ 1,28
Accrued Depreciation-Equipment	10,101,423				800,117		10,901,540	
Other Unadjusted Credits	4,436,931				46,240	$ 4,383,255	99,916	9
Total Unadjusted Credits	$ 15,645,142				$ 1,023,683	$ 4,383,255	$ 12,285,570	$ 1,38
Corporate Surplus:								
Additions to Property through Income & Surplus	$ 420,553	$ 3,592			$ 28,878		$ 453,023	$
Profit and Loss-Balance	1,529,261	41,598			D 467,488	$ 942,824	160,547	114,35
Total Corporate Surplus	$ 1,949,814	$ 45,190			$ D 438,610	$ 942,824	$ 613,570	$114,35
Total Liabilities	$243,199,883	$5,340,839	$6,902,418	$503,941	$20,505,364	$28,308,852	$248,143,593	$237,19

NOTE: D - Deficit

September 25, 1936.

*The D.& R.G.W. R.R. Co. proportion-Contra taken to book April 1, 1936 - $75,960

	2,072,424	2,013,977	
10,850	81,240	61,240	
11,573	331,968	331,968	
	89,581	89,581	
37,001	1,258,195	1,258,195	
	2,953,014	2,953,014	
	6,411	6,411	
90,806	33,141	33,141	
	6,090	6,090	
50,230	$ 8,148,513	$ 8,186,388	
	$ 8,569	$ 8,569	
	189,446	189,446	
	$ 198,015	$ 198,015	
	$ 11,388	$ 11,388	
22,364	1,035,166	984,866	
22,364	$ 1,046,554	$ 996,254	
08,852	$248,143,593	$237,191,753	
74,082	$ 62,457,540	$ 200,000	
	16,445,600	33,621,940	
72,000	134,775,000	83,954,849	
	800,313	800,313	
47,352			
93,434	$214,478,453	$118,577,122	
10,850	$ 6,964,589	$ 35,000	
11,573	516,066	516,066	
53,852	1,445,949	1,395,648	
	40,291	40,292	
	7,509,470	380,495	
	2,003,000	3,000	
72,258	1,827,456	49,559	
40,806	53,106	53,106	
	22,548	22,548	
89,339	$ 20,382,475	$ 2,495,714	
	$ 383,525	$ 383,525	
	$ 383,525	$ 383,525	
	$ 1,284,114	$ 1,284,114	
	10,901,540	-	
83,255	99,916	99,916	
83,255	$ 12,285,570	$ 1,384,030	
	$ 453,023	$ -	
42,824	160,547	114,351,362	
42,824	$ 613,570	$114,351,362	
08,852	$248,143,593	$237,191,753	

The Denver and Rio Grande Western Railroad Company											
Accounts Receivable:											
Rio Grande Southern Railroad Company-Contra Account				$459,068							
The Denver and Salt Lake Railway Company				986							
Denver and Salt Lake Western Railroad Company				75,218							
The Denver and Rio Grande Western Railroad Company											
Other Unadjusted Debits:											
Deferred Payments-Bond Coupons-Contra Account						$5,328,985					
Refunding & Improvement Mortgage - Sinking Fund Contra Account						165,192					
The Denver and Rio Grande Western Railroad Company, Wilson McCarthy and Henry Swan, Trustees, Contra Account						2,737,867					
General Mortgage Sinking Fund-Contra Account						1,192,320					
The Denver and Rio Grande Western Railroad Company											
Traffic and Car Service Balances Receivable:											
The Denver and Salt Lake Railway Company			$ 2,025								
The Denver and Salt Lake Railway Company											
Traffic and Car Service Balances Receivable:											
The Denver and Rio Grande Western Railroad Company			9,548								
The Denver and Salt Lake Railway Company											
Miscellaneous Accounts Receivable:											
The Denver and Rio Grande Western Railroad Company				64,275							
The Denver and Salt Lake Railway Company											
Rents Receivable:											
The Denver and Rio Grande Western Railroad Company					$32,473						
The Denver and Salt Lake Western Railroad Company											
Loans and Bills Receivable:											$3,1
The Denver and Rio Grande Western Railroad Company		$3,110,850									
The Denver and Salt Lake Western Railroad Company											
Miscellaneous Accounts Receivable:											
The Denver and Rio Grande Western Railroad Company				145,476							
Rio Grande Junction Railway Company											
Rents Receivable:											
The Denver and Rio Grande Western Railroad Company					58,333						
Total Eliminations - Column 6	$14,936,258	$3,110,850	$11,573	$787,001	$90,806	$9,422,364		$11,074,082	$2,172,000	$747,552	$3,

A - Amounts Added

September 26, 1936.

THE DENVER AND RIO GRANDE WESTERN SYSTEM
PROPOSED PLAN OF CONSOLIDATION AND REORGANIZATION AS OF JANUARY 1, 1937
FINANCE DOCKET NO. 11002

Inter-Company Items Eliminated from Consolidated Balance Sheet (Column 6)

	Amounts Eliminated From Asset Accounts						Amounts Eliminated				
	Investments in Affiliated Companies	Loans and Bills Receivable	Traffic and Car Service Balances Receivable	Miscellaneous Accounts Receivable	Rents Receivable	Other Unadjusted Debits	Capital Stock: Preferred	Capital Stock: Common	Funded Debt	Nonnegotiable Debt to Affiliated Companies	Loans and Bill Payable
The Denver and Rio Grande Western Railroad Company											
Investments in Affiliated Companies:											
Rio Grande Junction Railway Company											
Stock	$ 720,990										
Bonds	906,000							$2,000,000			
Advances	278,951								$ 906,000		
Denver and Salt Lake Railway Company										$278,951	
Stock	7,838,356										
Bonds	1,042,560							5,323,082			
Denver and Salt Lake Western Railroad Company									1,256,000		
Stock	5,631,000										
Advances	14,460							5,631,000			
Goshen Valley Railroad Company										14,460	
Stock	488,861										
Advances	15,080							80,000		438,861	
										15,080	
The Denver and Rio Grande Western Railroad Company											
Accounts Receivable:											
Rio Grande Southern Railroad Company-Contra Account				$459,068							
The Denver and Salt Lake Railway Company				966							
Denver and Salt Lake Western Railroad Company				75,218							
The Denver and Rio Grande Western Railroad Company											
Other Unadjusted Debits:											
Deferred Payments-Bond Coupons-Contra Account						$5,322,985					
Refunding & Improvement Mortgage - Sinking Fund Contra Account						165,192					
The Denver and Rio Grande Western Railroad Company, Wilson McCarthy and Henry Swan, Trustees, Contra Account						2,737,867					
General Mortgage Sinking Fund-Contra Account						1,192,320					
The Denver and Rio Grande Western Railroad Company											
Traffic and Car Service Balances Receivable:											
The Denver and Salt Lake Railway Company			$ 2,025								
The Denver and Salt Lake Railway Company											
Traffic and Car Service Balances Receivable:											
The Denver and Rio Grande Western Railroad Company			9,548								
The Denver and Salt Lake Railway Company											
Miscellaneous Accounts Receivable:											
The Denver and Rio Grande Western Railroad Company				64,273							
The Denver and Salt Lake Railway Company											
Rents Receivable:											
The Denver and Rio Grande Western Railroad Company					$32,473						
The Denver and Salt Lake Western Railroad Company											
Loans and Bills Receivable:											
The Denver and Rio Grande Western Railroad Company		$3,110,850									$3,110,8
The Denver and Salt Lake Western Railroad Company											
Miscellaneous Accounts Payable											

Exhibit 23a

Witness Hm. Hyer

[illegible]Y 1, 1937

[illegible] (Column 6)

Amount Eliminated from Liability Accounts

[illegible]ded Debt	Nonnegotiable Debt to Affiliated Companies	Loans and Bills Payable	Traffic and Car Service Balances Payable	Audited Accounts and Wages Payable	Unmatured Interest Accrued	Unmatured Rents Accrued	Other Unadjusted Credits-Contra	Profit and Loss
								A $1,279,010
906,000								
	$278,951							
								2,445,274
1,266,000								A 223,440
	14,460							
	438,861							
	15,080							
							$ 453,068	
				$ 966				
				73,218				
				5,328,985				
				163,192				
							2,737,867	
							1,192,330	
			$ 2,025					
			9,548					
				64,273				
						$ 32,473		
		$3,110,850						

				$ 966				
				73,218				
				5,328,985				
				163,192				
							2,737,867	
							1,192,320	
			$ 2,025					
			9,548					
				64,273				
						$ 32,475		
		$3,110,850						
				73,218	$72,258			
				50,000		8,533		
2,172,000	$747,352	$3,110,850	$11,573	$5,703,852	$72,258	$40,906	$4,[illegible]3,255	$94[illegible],824

[fol. 1482] EXHIBIT 27

Witness Wm. Wyer

The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937, Finance Docket No. 11002

Capitalizable Assets December 31, 1935

The Denver and Rio Grande Western Railroad Company
The Rio Grande Junction Railway Company

In Finance Docket 9754 (189 ICC 665) the ICC authorized the issuance of D&RGW bonds based on additions and betterments made on the properties of the D&RGW and RGJct. Rwy. prior to December 31, 1931, as of which date the Investment in Road and Equipment of these two companies, was		
D&RGW	$212,187,494	
RGJct	5,192,279	
		$217,379,773
Of the expenditures prior to 1932 the following were not included in Form A submitted at that time.		
D&RG	$ 5,677,149	
RGJct	3,955	
		5,681,104
		$211,698,669
Of the expenditures prior to December 31, 1931 the ICC did not allow as properly capitalizable expenditures (See Report FD 9751-1. 189 I. C. C. 665)		
D&RG	$ 72,952	
RGJct	11,243	
		84,195
		$211,614,470

Goshen Valley Railroad Company

In Finance Docket 6205-1 the ICC approved acquisition of Goshen Valley stock (124 ICC 397). The purchase price was set forth as $488,861.12 representing the cost of construction and of the right of way.. This was the value assigned to this stock on the D&RGW balance sheet.	488,861
	$212,103,331

The Denver and Salt Lake Western Railroad Company

In Finance Docket 9720 (189 ICC 181) the ICC approved issuance of $3,850,000 of stock for estimated cost of construction of the line of which there was spent	3,631,000
	$215,734,331

[fol. 1483] *The Denver and Salt Lake Railway Company*

In Finance Docket 8070 (170 ICC 4 and 175 ICC 542) there was submitted a balance sheet of the D&SL Rwy. as of October 31, 1929 showing		
Investment in Road and Equipment	$ 16,515,634	
Improvements on Leased Railway Property	32,540	
In this Docket the ICC authorized acquisition of the D&SL stock at $155 per share or for the 50,000 shares outstanding		$7,750,000
As of October 31, 1929 the D&SL Rwy. also had outstanding Long Term Debt of		13,500,000
A total capitalizable value of		$ 21,250,000
Total all companies, excluding amounts represented by Forms A herewith		$236,984,331

[fol. 1464] Forms A Herewith

D&RGW		
Road and Equipment 1-1-1932 to 12-31-35	$1,283,660	Cr
do prior to 1932	5,677,149	
	$ 4,393,489	
Improvements on Moffat Tunnel Improvement District November 1, 1934 to December 31, 1935	399,423	
Improvements on D&SLW January 1 to December 31, 1935	14,460	
D&SL Rwy.		
Road and Equipment July 1, 1933 to December 31, 1935	802,980	Cr
Improvements on Leased Railway Property July 1, 1933 to December 31, 1935	253,903	
RGJct		
Road and Equipment 1-1-32 to 12-31-35	33,632	
do prior to 1932	3,955	
Goshen Valley		
Road and Equipment 5-1-28 to 12-31-35	15,080	
Total Forms A	$ 4,310,962	

Grand Total Capitalizable Investment as of December 31, 1935 $241,295,293

October 17, 1936

[fol. 1485] EXHIBIT 28

Witness Wm. Wyer

The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937

Finance Docket No. 11002

Description of Obligations and Their Security

October 15, 1936.

[fol. 1486] The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization, as of January 1, 1937

Finance Docket No. 11002

Description of Obligations and Their Security

The Denver and Rio Grande Western Railroad Company

1. Equipment Trust, Series A, dated March 1, 1923, Supplemental Lease, dated July 1, 1924.

Trustee: The Pennsylvania Company for Insurances on Lives and Granting Annuities, Philadelphia, Pa.

Principal amount of certificates authorized by indenture: $4,500,000.

Amount outstanding in hands of public, December 31, 1936: $600,000.

Maturity: $300,000 annually, March 1, 1937 and 1938.

Interest rate: 5½%.

I. C. C. Authorization: F. D. 2872, 69 ICC 182.

Security, as of December 31, 1935: 50 locomotives, 1594 freight train cars, 45 work equipment.

Cost of original equipment: $6,133,857.

2. Equipment Trust, Series B, dated March 1, 1926.

Trustee: The Pennsylvania Company for Insurances on Lives and Granting Annuities, Philadelphia, Pa.

Principal amount of certificates authorized by indenture: $1,725,000.

Amount outstanding in hands of public, December 31, 1936: $575,000.

Maturity: $115,000 annually, March 1, 1937 to March 1, 1941.

Interest rate: 5%.

I. C. C. Authorization: F. D. 5418, 105 ICC 785.

Security, as of December 31, 1935: 10 locomotives, 200 automobile cars, 500 steel gondola cars.

Cost of original equipment: $2,314,473.

3. Equipment Trust, Series C, dated May 1, 1927.

Trustee: The Pennsylvania Company for Insurances on Lives and Granting Annuities, Philadelphia, Pa.

[fol. 1487] Principal amount of certificates authorized by indenture: $1,575,000.

Amount outstanding in hands of public, December 31, 1936: $630,000.

Maturity: $105,000 annually, May 1, 1937, to May 1, 1942.

Interest rate: 4½%.

I. C. C. Authorization, F. D. 6227, 124 ICC 383.

Security, as of December 31, 1935: 10 locomotives, 4 dining cars, 300 automobile cars.

Cost of original equipment: $2,114,569.

4. The Rio Grande Western Railway Company First Trust Mortgage, dated July 1, 1889.

Supplemental indentures as follows: March 24, 1899; January 28, 1902; December 20, 1924; April 1, 1925; March 29, 1932.

Trustee: Central Hanover Bank & Trust Company, New York, N. Y.

Principal amount of bonds authorized by indenture	$16,000,000
Amount issued, December 31, 1935:	
Outstanding in hands of public	15,190,000
Pledged with Reconstruction Finance Corporation	10,000
	$15,200,000

Date of maturity: July 1, 1939.

Interest rate: 4%.

I. C. C. Authorization:

$15,190,000 outstanding: issuance not authorized. Liability assumed by D&RGW pursuant to F. D. 3169, 82 ICC 745.

10,000 pledged: Issuance and assumption by D&RGW authorized in F. D. 9323, 184 ICC 425. Pledge authorized in F. D. 9181, 180 ICC 777.

Present security: A first lien on approximately 415 miles of railroad, 314 miles of which constitutes the main line of the D&RGW from Crevasse (near Colorado-Utah state line) to Ogden, Utah. Also a first lien on a small amount of equipment as set forth in separate exhibit.

5. The Denver and Rio Grande Railroad Company First Consolidated Mortgage, dated July 15, 1886.

Supplemental indentures as follows: March 27, 1890; April 14, 1890; January 26, 1891; May 20, 1891; September 11, 1891; January 30, 1894; June 9, 1916; December 20, 1924; April 1, 1925; March 29, 1932.

Trustee: United States Trust Company, New York, N. Y.

Principal amount of bonds authorized by indenture: $42,000,000.

Amount issued, as of December 31, 1935:

Outstanding in hands of public	4%	$34,125,000	
	4½%	6,382,000	$40,507,000
Pledged with:			
Reconstruction Finance Corporation	4%	783,000	
The Railroad Credit Corporation	4%	662,000	1,445,000
			41,952,000

[fol. 1488] Date of maturity: January 1, 1936.

I. C. C. Authorization:

$40,507,000 outstanding: Issuance not authorized. Liability assumed by D&RGW pursuant to F. D. 3169, 82 ICC 745.

783,000 pledged with RFC: Issuance and assumption by D&RGW authorized in F. D. 9323, 184 ICC 425. Pledge authorized in F. D. 9181, 180 ICC 777.

662,000 pledged with RCC: Issuance and assumption by D&RGW and pledge authorized in F. D. 9323, 184 ICC 425.

Present security: A first lien on approximately 875 miles of standard gauge and 683 miles of narrow gauge railroad (counting three-rail line from Hooper to Antonito as narrow gauge), practically all of which is in Colorado. Prin-

cipal line, Denver via Pueblo to Rifle, 386 miles. Also a first lien on certain equipment, as set forth in separate exhibit.

6. The Rio Grande Western Railway Company First Consolidated Mortgage, dated April 1, 1899.

Supplemental indentures as follows: June 1, 1899; October 10, 1899 (3); January 19, 1900; January 29, 1900; January 30, 1900; March 19, 1901; April 13, 1901; May 23, 1901; July 20, 1908 (6); January 21, 1910 (2); February 13, 1929; December 20, 1924; April 1, 1925; March 29, 1932.

Trustee: Guaranty Trust Company of New York, N. Y.

Principal amount of bonds authorized by indenture: $28,200,000, plus $20,000 per mile of road constructed.

Amount issued as of December 31, 1935:

Outstanding in hands of public	$15,080,000	
Pledged with Reconstruction Finance Corporation	1,395,000	$16,475,000

Date of maturity: April 1, 1949.

Interest rate: 4%.

I. C. C. Authorization:

$15,080,000 outstanding: Issuance not authorized. Liability assumed by D&RGW pursuant to F. D. 3169, 84 ICC 745.

1,395,000 pledged: Issuance and assumption by D&RGW authorized in F. D. 9323, 184 ICC 425. Pledge authorized in F. D. 9181, 180 ICC 777.

Present security: A first lien on approximately 283 miles of standard gauge branch line railroad in Utah; on the entire capital stock of the Utah Fuel Company; and on certain equipment, as set forth in separate exhibit.

A second lien upon the property formerly owned by the Rio Grande Western Railway Company, subject only to its First Trust Mortgage.

[fol. 1489] 7. D&RGW Refunding and Improvement Mortgage, dated February 1, 1924.

Supplemental indentures as follows:

December 20, 1924

February 13, 1929.

January 29, 1930

Trustee: Chase National Bank of the City of New York.

Principal amount of bonds authorized by indenture: $150,000,000

Amount issued as of December 31, 1935:

Series A, 6% Bonds, due October 1, 1974, outstanding $2,000,000 ($1,000,000 owned by the Missouri Pacific Railroad Company and Western Pacific Railroad Corporation each.)

Series B, 5% Bonds, due April 1, 1978:

Outstanding in hands of public	$12,000,000	$14,000,000
Pledged with—Reconstruction Finance Corporation	4,385,000	
The Chase National Bank	6,096,000	10,481,000
Total Series B	22,481,000	
Total Both Series		$24,481,000

I.C.C. Authorization:

Series A: F.D. 3169, 90 ICC 141; F.D. 4377, 94 ICC 71.

Series B: F.D. 6806, 138, ICC 621; F.D. 7901, 158 ICC 301; F.D. 8271, 162 ICC 748; F.D. 9754, 189 ICC 665; F.D. 9181, 180 ICC 777.

Present security: A first lien on approximately 85 miles of standard gauge and 34 miles of narrow gauge branch lines in Colorado and Utah. Also a lien generally on all the lines of railroad and equipment owned by the D&RGW, subject only to prior liens, and a collateral lien on the Rio Grande Junction Railway, subject to its First Mortgage.

The following securities are pledged under the mortgage:

Terminal Companies:

*$4,800 par value capital stock of Denver Union Terminal Company (⅛ of total issue.)

8,000 par value capital stock of Pueblo Union Depot and Railroad Co. (of total of $40,600 issued.)

99,500 par value Salt Lake City Union Depot and Railroad Company (½ of total issue.)

(Directors' qualifying shares of above companies, owned by D&RGW, are not pledged. Are included in showing per cent of total issue owned by D&RGW.)

[fol. 1490] Rio Grande Junction Railway Company:

$1,999,300 par value capital stock. (D&RGW owns total issue of 20,000 shares, including seven directors' qualifying shares unpledged.)

*Subject to prior pledge under stock trust agreement.

906,000 principal amount Refunding Bonds. (Total amount issued under mortgage.)

Miscellaneous:

$8,335,000 principal amount DRG Improvement Mortgage Bonds due June 1, 1928, held as muniment of title. Bonds paid at maturity (except $2,000. for which cash is deposited) but mortgage not released of record.

8. Reconstruction Finance Corporation Notes:—

For general corporate purposes—6%:

Date	Amount	Maturity	I.C.C. Authorization
March 29, 1932	$250,000	March 29, 1935	F.D. 9181, 180 ICC 777
June 27, 1932	750,000	March 29, 1935	F.D. 9181, 180 ICC 777
July 29, 1932	1,000,000	March 29, 1935	F.D. 9181, 180 ICC 777
April 25, 1933	1,000,000	Demand	
June 30, 1933	950,000	Demand	(F. D. 9777, 189 ICC 674) 193 ICC 209
	$3,950,000		

For construction of D&SLW (Cutoff)—5%

January 12, 1933	$ 105,500	January 12, 1936 F. D. 9562, 187 ICC 399
February 2, 1933	91,800	February 2, 1936
February 25, 1933	81,500	February 25, 1936
March 22, 1933	88,800	March 22, 1936
April 20, 1933	219,700	April 20, 1936
May 20, 1933	297,800	May 20, 1936
June 26, 1933	231,900	June 26, 1936
July 20, 1933	197,600	July 20, 1936
August 22, 1933	281,800	August 22, 1936
September 22, 1933	472,000	September 22, 1936
October 20, 1933	357,700	October 20, 1936
November 20, 1933	201,600	November 20, 1936
December 21, 1933	189,800	December 21, 1936
January 16, 1934	163,500	January 16, 1937
February 21, 1934	91,200	February 21, 1937
March 21, 1934	85,800	March 21, 1937
April 30, 1934	115,300	April 30, 1937
June 11, 1934	165,700	June 11, 1937
June 26, 1934	99,000	June 26, 1937
August 6, 1934	57,500	August 6, 1937
August 31, 1934	46,500	August 31, 1937
	$3,631,000	

[fol. 1491] For acquisition of D&SL capital stock—5%: December 19, 1934 $3,182,150 Demand F. D. 10634, 202 ICC 489

Less credit of	71,300
	3,110,850
Total Debt	$10,691,850

Notes are secured by following collateral:

Description	Par Value
D&RGW Bonds:	
D&RG First Consolidated 4% Bonds	$ 783,000
RGW First Trust 4% Bonds	10,000
RGW First Consolidated 4% Bonds	1,395,000
D&RGW Refunding and Improvement 5% Bonds	4,385,000
Cutoff Securities:	
D&SL Income 6% Bonds (Total Issue, $11,000,000)	1,266,000
D&SL Capital Stock, no par (49,540 shares out of total issue of 50,000) cost to D&RGW	7,838,355
D&SLW Capital stock (total issue)	3,631,000
Motorway Stocks:	
Denver—Colorado Springs—Pueblo Motor Way, Inc., capital stock (½ of total issue) (par value $1, per sh)	42,000
Rio Grande Motor Way, Inc., capital stock (80% of entire issue) (par value $100. per share)	130,000
Miscellaneous:	
Goshen Valley Railroad Stock (500 shares, entire issue)	50,000
Rio Grande Southern Railroad Company First Mortgage 4% Bonds (in default since 1922)	1,777,000

Second lien on securities pledged with:

(a) The Railroad Credit Corporation

(b) The Chase National Bank for loans.

9. The Railroad Credit Corporation Note:

Note for $500,000, dated June 1, 1932, payable on demand or March 31, 1934

Interest rate: 1-½%, adjusted quarterly to rediscount rate of Federal Reserve Bank, New York.

Secured by:

(a) $662,000 principal amount, D&RG First Consolidated 4% Bonds;

(b) D&RGW's share in Marshalling and Distributing Fund;

(c) Second lien on securities pledged with Reconstruction Finance Corporation.

[fol. 1492] 10. Bank Debt:

Note for $1,500,000, dated April 30, 1935, payable on demand to The Chase National Bank of the City of New York.

Interest rate: 5%.

Secured by $6,096,000 principal amount, D&RGW Refunding and Improvement Mortgage 5% Bonds.

11. D&RGW General Mortgage, dated February 1, 1924.

Trustee: City Bank Farmers Trust Company, New York.

Principal amount of bonds authorized and outstanding, December 31, 1935: $29,808,000.

Date of maturity: August 1, 1955.

Interest rate: 5%.

Sinking fund: 1% of maximum principal amount of bonds at any time outstanding, if Net Income sufficient for payment.

I.C.C. Authorization: F.D. 3169, 82 ICC 745; 90 ICC 141.

Security: A lien generally upon the property of the D&RGW securing the Refunding and Improvement Mortgage, but junior thereto.

12. D&RGW Trustees' Certificates.

	Series A	Series B
Principal amount	$1,000,000	$650,000
Date of issue	July 31, 1936	July 31, 1936
Date of maturity	December 31, 1936	April 30, 1937
Rate of interest	1-½%	2%

I.C.C. Authorization: Report and order dated July 23, 1936, F.D. 11271.

Security: Both series equally secured by a first and paramount lien (except and subject to liens for taxes and assessments and the rights of trustees under any equipment trusts in respect of equipment subject thereto) upon the property of the D&RGW, and upon surplus earnings. For further detail, see Court Proceedings, p. 1658.

The Denver and Salt Lake Western Railway Company

13. Reconstruction Finance Corporation Note:

Note for $3,182,150 (later reduced by credit of $71,300 to $3,110,850) dated December 19, 1934, payable to Reconstruction Finance Corporation on demand:

Interest rate: 5%

Secured by note of D&RGW in same amount, payable to bearer, and collaterally secured by 40,140 shares of D&SL capital stock.

The Denver and Salt Lake Railway Company

14. First Mortgage, dated January 1, 1927.

Trustee: Bankers Trust Company of New York.

[fol. 1497] Principal Amount of Bonds Authorized by indenture: $11,000,000.

Amount outstanding in hands of public, December 31, 1936: $1,500,000.

Date of maturity: January 1, 1950.

Rate of interest: 4%.

Present security: First lien on entire property of company, including line of railroad from Utah Junction (Denver) to Craig, Colorado, and lease of Moffat Tunnel.

15. Income Mortgage, dated January 1, 1927.

Trustee: International Trust Company, Denver, Colorado.

Principal amount of bonds authorized by indenture and outstanding in hands of public as of December 31, 1936: $11,000,000. ($1,266,000 owned by D&RGW and pledged with RFC.)

Date of Maturity: January 1, 1960.

Interest provisions: Interest payable only if earned, in multiples of 1%, with maximum rate of 6% per annum. Interest is cumulative to the extent of 75% of the Company's net income in any year.

Present security: A lien on the property of the company subject to the lien of the First Mortgage, but junior thereto.

Rio Grande Junction Railway Company.

16. First Mortgage, dated December 1, 1889.

Trustee: Control Hanover Bank and Trust Company.

Principal amount of bonds authorized and outstanding: $2,000,000.

Date of maturity: December 1, 1939.

Interest rate: 5%.

I. C. C. Authorization: Issuance not authorized. Liability assumed by D&RGW pursuant to F. D. 3169, 82 ICC 745.

Present security: A first lien on the line of railroad extending from Rifle to Grand Junction, Colorado, 62.08 miles.

17. Refunding Mortgage, dated January 1, 1929.

Trustee: The Equitable Trust Company of New York.

Principal amount of bonds authorized: $12,000,000.

Amount issued as of December 31, 1935: $906,000.

(All owned by D&RGW and pledged under its Refunding and Improvement Mortgage.)

Date of maturity: January 1, 1979.

Interest rate: 5%.

I. C. C. Authorization: as to $718,000—F.D. 7570, 158 ICC 314
as to $188,000—F.D. 9754, 189 ICC 665

$906,000

Present security: A lien upon the property of the RGJ, subject only to the lien of the RGJ First Mortgage.

[fols. 1494-1495] EXHIBIT NO. 34

* * * * * * *

WESTERN CONSOLIDATED MORTGAGE. SUBDIVISION IV OF ARTICLE FIRST

IV. —The Railway Company hereby covenants to use the proceeds of the bonds which shall be issued pursuant to subdivisions II and III, or either of them, of this First Article, to pay for the building, purchase or other acquisition or equipping of railroad which shall or may constitute a branch or branches or extension or extensions of the railroad of the Railway Company, or to pay for the acquisition of securities of companies which shall own railroad which shall or may constitute such branch or branches, extension or extensions, or to pay for the development of property of

the Railway Company by providing for its necessities for equipment or other improvements of, or additions to, its property, or to pay for acquisitions lawfully made with a view of increasing its traffic or earnings.

[fol. 1496] EXHIBIT 34J

Witness Wm. Wyer

The Denver and Rio Grande Western Railroad System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937. Finance Docket No. 11002

Copy made September 18, 1936 of original on file with Guaranty Trust Company of New York.

An Agreement, made and entered into this twenty-third day of May, 1901, by and between Spencer Trask & Company, the Rio Grande Western Railway Company and the Morton Trust Company, as Trustee under the consolidated mortgage of said Railway Company, dated April 1, 1899.

Whereas, said Spencer Trask & Company are the owners of the entire capital stock of the Utah Fuel Company and the same has been deposited by them with the Morton Trust Company as Trustee as aforesaid.

Now, Therefore, for valuable consideration, the parties hereto hereby agree to and with each other as follows:

The said stock shall be held by the said Morton Trust Company as such Trustee as security for the payment of the principal and interest of the bonds of the said Rio Grande Western Railway Company secured by said first consolidated mortgage and in all respects subject to the terms and conditions of said Mortgage with reference to the railroad securities pledged thereunder, and upon the further condition that the Western Company shall have the right, at any time, upon paying to the Trustee six million dollars in cash, or upon delivering to the Trustee said first consolidated mortgage bonds to the amount of six million dollars at par, with all accrued coupons attached, to receive the said stock of the Utah Fuel Company free and discharged from the lien of the said mortgage. Subject to the first [fol. 1497] and prior lien thereof, the said stock is hereby transferred and assigned to the said Rio Grande Western Railway Company.

In Witness Whereof, the parties hereto have signed their names and affixed their Seals the day and year first above written.

(Signed) Spencer Trask & Co. The Rio Grande Western Ry. Co., By Wm. J. Palmer, President.
Attest: (Sgd.) Geo. A. Krause, Secretary. (Seal.)

Morton Trust Company (Signed) By J. D. Corbecne, 2d Vice Prest.
Attest (Sgd.) H. M. Francis, Secretary. (Seal.)

[fol. 1498] EXHIBIT 35—WITNESS WM. WYER

The Denver and Rio Grande Western System Proposed Plan of Consolidation as of January 1, 1937

Finance Docket No. 11002

The Western Pacific Railroad Corporation
The Denver and Rio Grande Western Railroad Company
Missouri Pacific Railroad Company
and
James S. Alexander, as Trustee

AGREEMENT

Relating to the Stock of Utah Fuel Company

Dated December 20, 1924

[fol. 1499] Agreement dated the 20th day of December, 1924, between The Western Pacific Railroad Corporation, a Delaware corporation (hereinafter called the Western Pacific), The Denver and Rio Grande Western Railroad Company, a Delaware corporation (hereinafter called the Denver Company), Missouri Pacific Railroad Company, a Missouri corporation (hereinafter called the Missouri Pacific) and James S. Alexander, as Trustee (hereinafter called the Trustee).

The Rio Grande Western Railway Company heretofore executed its First Consolidated Mortgage Deed, dated April 1, 1899, to The State Trust Company, Trustee (hereinafter called the Consolidated Mortgage) and thereafter

executed an Agreement, dated, May 23, 1901, (hereinafter called the Pledge Agreement), with Spencer Trask & Company and Morton Trust Company (the then trustee of the Consolidated Mortgage) pledging to said Trust Company as such trustee, to be held upon the terms in said Agreement set forth, 100,000 shares of the capital stock of Utah Fuel Company, a New Jersey corporation, constituting the entire capital stock of said Company.

On June 20, 1918, all of the right, title and interest of the Denver and Rio Grande Railroad Company (a successor in title to said The Rio Grande Western Railroad Company) in and to said 100,000 shares of the capital stock of Utah Fuel Company was sold under execution and purchased by William Salomon & Company and the right, title and interest of William Salomon & Company in and to said shares of stock was subsequently transferred to the Western Pacific. Thereafter, in a suit pending in the District Court of the United States for the District of Colorado, wherein The Equitable Trust Company of New York, as Trustee, was Intervenor and substituted Plaintiff and The Denver and [fol. 1500] Rio Grande Railroad Company was Defendant (In Equity No. 6782), by decree of said court said sale on execution was confirmed, and, by deed executed by the Special Master appointed in said suit, the Receiver appointed therein, and said The Denver and Rio Grande Railroad Company any right, title, and interest, if any, remaining in said The Denver and Rio Grande Railroad Company or its receiver in or to said stock was assigned and transferred to the Western Pacific. Pursuant to said decree in said suit, any remaining interest in or claim to said stock on the part of said The Denver and Rio Grande Railroad Company, if any, also was sold and thereafter was assigned and transferred by the purchasers thereof to, and became vested in, the Western Pacific.

Thereafter, pursuant to an order made and entered November 20, 1924, by the District Court of the United States for the District of Colorado in a cause therein pending entitled "Bankers Trust Company, as Trustee, Plaintiff against The Denver and Rio Grande Railroad Company and The Denver and Rio Grande Western Railroad Company, Defendants, in Equity, No. 7381, Consolidated Cause", confirming a sale in foreclosure made in said cause pursuant to a final decree duly entered therein, September 18, 1924, Cass E. Herrington, Special Master appointed in

said cause, T. H. Beacom, Receiver, Bankers Trust Company, as Trustee under the First and Refunding Mortgage of the Denver and Rio Grande Railroad Company, and The New York Trust Company, as Trustee under the Adjustment Mortgage of The Denver and Rio Grande Railroad Company, and Donald C. Swatland and Hayward A. Hibberd, the purchasers at said sale, by deed dated as of December 1, 1924, duly assigned and transferred to the Denver Company all title, equity, interests, rights, rights of subrogation and/or marshalling, and claims and demands, if any, of said Bankers Trust Company, as Trustee under said First and Refunding Mortgage, and of said [fol. 1501] The New York Trust Company, as Trustee under said Adjustment Mortgage, in or to or in respect of said stock of Utah Fuel Company, or dividends paid or declared thereon, or in or to or in respect of any cause of action connected therewith. The Denver Company has released to the Western Pacific and to The Guaranty Trust Company of New York, the present Trustee under the Consolidated Mortgage, any right or claim, if any, to any dividend or dividends paid in respect of the Utah Fuel Company stock after June 20, 1918, and prior to the date hereof.

It is provided in the Plan and Agreement dated June 15, 1923, for the Reorganization of the Denver and Rio Grande Western Railroad System, as modified February 29, 1924, (hereinafter called the Reorganization Plan), that the interest of the Western Pacific, and any interest which might thereafter be acquired by the Denver Company in said stock of Utah Fuel Company, subject to the pledge of said stock under the Consolidated Mortgage in accordance with the Pledge Agreement, with any rights of redemption which appertain thereto, shall be transferred to a trustee or trustees upon the terms in the Reorganization Plan provided.

The certificates for said shares of stock of Utah Fuel Company are in the possession of said The Guaranty Trust Company of New York, as Trustee under the Consolidated Mortgage, and are registered in the name of said Trust Company or of its nominees.

The parties, other than the Trustee have knowledge of the terms of the Consolidated Mortgage, the Pledge Agreement and the Reorganization Plan. The Trustee assumes no responsibility for the correctness of any of the foregoing recitals.

Now, therefore, in consideration of the premises and of the sum of one dollar to each of them paid, the Western Pacific and the Denver Company hereby respectively sell, [fol. 1502] assign, transfer and set over to James S. Alexander, as Trustee, all of their right, title and interest in and to said 100,000 shares of the capital stock of Utah Fuel Company, subject, however, to the pledge thereof under the Consolidated Mortgage, together with all rights of redemption of said 100,000 shares of capital stock of Utah Fuel Company arising through the Pledge Agreement.

And it is hereby agreed that the said right, title and interest in and to said stock of Utah Fuel Company and said rights of redemption shall be held by the Trustee, subject to the conditions, upon the limitations, and for the uses and purposes herein set forth.

First: The Western Pacific hereby assigns and transfers to the Missouri Pacific, subject to the Consolidated Mortgage, and to the provisions of this agreement, and the rights of the Trustee hereunder, one-half its right, title and interest in, to or in respect of the Utah Fuel Stock.

The Denver Company hereby assigns and transfers to the Western Pacific and the Missouri Pacific, in equal shares, subject as aforesaid, all its right, title and interest in, to or in respect of the Utah Fuel Stock. The ultimate beneficial interest in said 100,000 shares of the capital stock of Utah Fuel Company (hereinafter called the Utah Fuel Stock) shall be vested one-half in the Missouri Pacific and one-half in the Western Pacific.

Second: The Trustee shall cause all dividends that shall be declared and paid on the Utah Fuel Stock prior to February 1, 1929, to be paid to the Denver Company, and shall execute and deliver, or request Guaranty Trust Company of New York, as trustee under the Consolidated Mortgage, to execute and deliver, all proper dividend orders for that purpose. Any such dividends received by the Trustee prior to said date shall forthwith be paid over to the Denver Company. From and after February 1, 1929, the Trustee [fol. 1503] from time to time, on the written request of the Denver Company, or the Missouri Pacific, or the Western Pacific or the Preferred Stockholders Committee created as provided in the Reorganization Plan (hereinafter called the Preferred Stockholders Committee) accompanied by

the certificate hereinafter provided for, shall execute and deliver, or request Guaranty Trust Company of New York, as trustee as aforesaid, to execute and deliver, dividend orders in favor of the Denver Company so that, so long as any of the Bonds (hereinafter called the General Mortgage Bonds) secured by the General Mortgage of the Denver Company to the Farmers' Loan and Trust Company, Trustee, dated February 1, 1924, (hereinafter called the General Mortgage) or any of the Bonds (hereinafter called the Refunding Bonds) secured by the Refunding and Improvement Mortgage of the Denver Company to The Equitable Trust Company of New York, Trustee, dated February 1, 1924, (hereinafter called the Refunding Mortgage), or any bonds or obligations issued to pay or refund the General Mortgage Bonds or the Refunding Bonds, or any of them, are outstanding, dividends declared on the Utah Fuel Stock shall be paid, as the same are distributed, to the Denver Company; provided, however, that if at any time on or after February 1, 1929, the net income of the Denver Company, together with the dividends paid upon the Utah Fuel Stock, shall have been sufficient, during the preceding period of twelve calendar months, to pay the dividends accruing upon the preferred stock of the Denver Company for said period of twelve calendar months, and all arrears of dividends upon said preferred stock shall have been paid and money provided and appropriated for the payment of the dividends payable thereon during the next succeeding period of twelve calendar months, then so long as the net income of the Denver Company and the dividends upon the Utah Fuel Stock shall be more than sufficient [fol. 1504] to pay the dividends accruing upon the preferred stock of the Denver Company and no arrears of dividends thereon shall exist and so long as moneys shall be available and shall have been appropriated by the Denver Company for the payment of the dividend or dividends upon said preferred stock for a succeeding period of at least twelve calendar months and such dividends shall have been declared, the dividends on the Utah Fuel Stock, so far as the same shall not be required to provide for the payment of dividends upon said preferred stock as aforesaid, shall by the Trustee be directed to be and shall be paid to the Western Pacific and the Missouri Pacific, or their assigns, respectively, in equal shares, notwithstanding any request for the payment of such dividends to the Denver Company.

In case at any time no General Mortgage Bonds or Refunding Bonds or bonds or obligations issued to pay or refund the General Mortgage Bonds or the Refunding Bonds, or any of them, shall be outstanding, the Trustee, if this agreement shall remain in force thereafter, shall, on like request, execute and deliver, or request Guaranty Trust Company of New York, as trustee as aforesaid, to execute and deliver, dividend orders in favor of the Western Pacific and the Missouri Pacific, or their assigns, respectively, in equal shares.

Whenever, on or after February 1, 1929, any such request is made upon the Trustee for, or to procure, dividend orders with respect to dividends upon the Utah Fuel Stock, the corporation or committee making such request shall furnish to the Trustee a certificate signed by the Chairman of the Board, the President or a Vice-President and by the Treasurer or an Assistant Treasurer of the Denver Company setting forth (a) whether any General Mortgage Bonds or Refunding Bonds, or any bonds or obligations issued to pay or refund the General Mortgage Bonds or the Refunding Bonds, or any of them, are outstanding, and, if so, (b) the net income of the Denver Company, and the dividends paid upon the Utah Fuel Stock, during the twelve calendar [fol. 1505] months preceding the date of such certificate; (c) the aggregate par value of the preferred stock of the Denver Company then outstanding, and the aggregate amount of dividends which accrued thereon during the twelve calendar months preceding said date and the aggregate amount of dividends payable thereon during the twelve calendar months next succeeding said date; (d) the arrears of dividends, if any, upon said preferred stock; and (e) the provision and appropriation, if any, for the payment of the dividends upon said preferred stock for the twelve calendar months next succeeding said date, and whether any such dividends have been declared by the Denver Company.

The Trustee shall be entitled to act hereunder in reliance on any such certificate, and on the statements therein contained, and shall incur no liability for any such action.

Third: The Board of Directors of Utah Fuel Company shall consist of six directors and the Missouri Pacific and the Western Pacific shall each have the right to nominate

three of such directors. Any such nomination shall be made in writing and be delivered to the Trustee not less than ten days prior to any meeting of the stockholders of Utah Fuel Company for the election of a director or directors. If any such nomination is made, the Trustee shall cause the Utah Fuel Stock subject hereto to be voted for the election of the persons so nominated as directors. If and to the extent that no such nomination is made, the Trustee may vote the Utah Fuel Stock for the election of such directors as he may determine, but the Trustee shall at any time, at the joint request of the Missouri Pacific and the Western Pacific, vote the Utah Fuel Stock for the removal of any director or directors not nominated by either of said corporations, and for the election of the person or persons speci- [fol. 1506] fied in such request. The Trustee, so far as he may legally do so under its charter and by-laws and the statutes governing its incorporation, shall forthwith cause the by-laws of the Utah Fuel Company to be amended to provide in effect:

(a) that there shall be six members of the Board of Directors;

(b) that special meetings of stockholders may be called at any time by the holders of record of a majority in amount of the outstanding stock or by any director;

(c) that vacancies in the Board may be filled only by vote of the holders of record of two-thirds in amount of the outstanding stock;

(d) that any director not nominated by the Missouri Pacific or the Western Pacific may at any time be removed by vote of the holders of record of a majority in amount of the outstanding stock;

(e) that the members from time to time of the Preferred Stockholders Committee shall be entitled to receive copies of the minutes of meetings of the Board of Directors of Utah Fuel Company and that one member of said Committee, designated by said Committee, shall be privileged to attend all meetings of the Board of Directors of Utah Fuel Company, but without the right to vote thereat, and shall be entitled to receive fees for attending such meetings and/or reimbursement of

his personal expenses in connection therewith to the same extent as directors; and

(f) that the Preferred Stockholders Committee, at any time when as many as four quarterly dividends upon the preferred stock (whether or not consecutive) shall have accrued and be unpaid, may, and at the request in writing of the holders of record of at least [fol. 1507] ten per cent of the then outstanding preferred stock shall, appoint an accountant familiar with railroad affairs, a banker, and a man of experience in practical railroad work, who shall be given full access to the books and accounts of Utah Fuel Company.

Subject to the specific provisions of this agreement, the Trustee shall possess, in respect of the Utah Fuel Stock, and shall be entitled to exercise, all of the powers of absolute owner thereof and all rights of every name and nature in respect thereof, including the right to vote and consent for every purpose; provided, however, that subject to the provisions of this agreement, the Trustee shall at any time vote in such manner or take such other action as may from time to time be directed in writing by the Western Pacific and the Missouri Pacific jointly.

It shall be the policy of Utah Fuel Company, so long as this agreement shall remain in force, that surplus earnings and profits shall not be unreasonably accumulated in the treasury of that Company and, in voting the stock held by him hereunder (which may be done either in person or by proxy) and in acting on matters which may come before any stockholders meeting, the Trustee will endeavor to carry out said policy, and will otherwise exercise his best judgment; but the Trustee assumes no responsibility, except for the exercise of good faith, in respect of carrying out said policy or in respect of the management of said Company or in respect of any action taken by him or in pursuance of any consent by him as such stockholder or pursuant to his vote so cast, and the Trustee shall incur no responsibility by reason of any errors of law or judgment or any matter or thing done or omitted under this agreement, except for his own wilful malfeasance.

[fol. 1508] Fourth: The Trustee may without request, and if the Missouri Pacific or the Western Pacific in writing so request, shall, from time to time, in order to qualify

persons to act as directors of Utah Fuel Company as provided herein, request; The Guaranty Trust Company of New York, as Trustee under the Consolidated Mortgage, to sell to, and/or transfer into the name of, each of the persons nominated to be directors in any such request or, in the absence of such request, selected by the Trustee to be such directors, such number of shares not exceeding ten (10) of the stock of Utah Fuel Company held hereunder as may be so requested or determined; provided, however, that in making any such request upon The Guaranty Trust Company of New York, the Trustee shall request that the certificates for any shares transferred as aforesaid shall be deposited immediately with The Guaranty Trust Company of New York, as such Trustee, endorsed in blank or accompanied by a proper instrument of assignment and transfer in blank, duly executed, together, if any of said shares of stock shall have been sold to any such person or persons selected for directors, with a written agreement in form satisfactory to The Guaranty Trust Company of New York, as such Trustee, giving The Guaranty Trust Company of New York, as such Trustee, the right at any time to repurchase, for the trust estate of the Consolidated Mortgage and subject thereto for the Trustee hereunder, the shares of stock so sold at the original sale price thereof, with such interest, if any, as shall be specified in such agreement.

Fifth: In the event of the foreclosure or enforcement of the Refunding Mortgage, or of the General Mortgage, or of any mortgage or other indenture executed by the Denver Company to secure bonds or obligations issued to pay or refund the Refunding Bonds or the General Mortgage Bonds, or any of them, the Trustee, on written de- [fol. 1509] mand of the trustee or trustees of any such mortgage or mortgages, or other indenture or indentures, or on the written demand of the Preferred Stockholders Committee, and upon being indemnified to his satisfaction against any loss, damage or expense which may result from his compliance with any such request, shall offer for sale, and, after giving reasonable notice of not less than four weeks to the trustee or trustees of each of such mortgages and/or indentures and to each of the parties hereto, and publishing like notice in such manner and for such length

of time as the Trustee shall deem expedient, shall sell for the best obtainable price, at public auction, at any time and place to be determined by the Trustee, and otherwise as may be so determined, the right, title and interest of the Trustee and of the Missouri Pacific and the Western Pacific in the Utah Fuel Stock, and all right, title and interest of the Denver Company therein or in respect thereof, and/or hereunder, free and clear of any claim or demand with respect to said stock, or the avails thereof, or any dividends thereafter to be paid thereon, in favor of, or on the part of, any trustee or trustees under any of said mortgages or indentures or of the holders of any bonds or obligations secured by any thereof or of any holders of preferred stock of the Denver Company, or of any one claiming under any party hereto, whether the Utah Fuel Stock be then subject to the Consolidated Mortgage or free therefrom, provided, that if the Utah Fuel stock shall then be subject to the Consolidated Mortgage such sale shall be expressed to be subject to the Consolidated Mortgage, and shall cause the net proceeds of any such sale to be applied to the payment of the bonds or obligations secured by such mortgages or other indentures, respectively, in accordance with the relative priority of the lien of such mortgages or other indentures upon the railroad property of the Denver Company as the same shall be determined by, and in such manner as may be directed by, the Court [fol. 1510] in charge of such foreclosure proceedings, or if such enforcement is without court proceedings, as the Trustee under advice of disinterested counsel may determine. If the trustee or trustees under any such mortgage or other indenture or the Preferred Stockholders Committee shall so request, such sale of the Utah Fuel Stock and application of the proceeds thereof shall be made before the application to such payment of the property subject to such mortgages or other indentures, or the proceeds thereof. Any surplus of such proceeds remaining after payment in full of the bonds or obligations secured by said respective mortgages or other indentures shall be divided equally between the Missouri Pacific and the Western Pacific. Unless and until the Trustee shall have written notice to the contrary from one or more of the parties to this agreement, the Trustee may, for all purposes of this agreement, assume that there has been no foreclosure or enforcement of the Refunding Mortgage, or of the General

Mortgage, or of any mortgage or other indenture executed by the Denver Company to secure bonds or obligations issued to pay or refund the Refunding Bonds, or the General Mortgage Bonds, or any of them.

Sixth: The Trustee shall at any time, at the joint request in writing of the Missouri Pacific and the Western Pacific, and upon being indemnified to his satisfaction against any loss, damage or expense which may result from his compliance with any such request, sell the entire interest in the Utah Fuel Stock held hereunder, subject only to the charge thereon, if any, of the Consolidated Mortgage, at such price, or exchange the entire interest in said stock, subject only as aforesaid, for other property, on such terms, as may be authorized by the respective Boards of Directors of the Missouri Pacific and the Western Pacific and approved by the holders of record of a majority of the preferred stock of the Denver Company at the time outstand- [fol. 1511] ing either at a meeting duly called and held, or in writing without a meeting; the cash proceeds of any such sale, in the event that any Refunding Bonds or any General Mortgage Bonds or any bonds or obligations issued to pay or refund the Refunding Bonds or the General Mortgage Bonds, or any of them, shall then be outstanding, shall be paid to the Denver Company to be expended by it for any purpose for which Refunding Bonds of the Denver Company may be issued under the Refunding Mortgage, and any property received in exchange for such stock shall either be transferred to the Denver Company or, in the discretion of the Trustee, be retained by him subject to all the provisions hereof; provided, that no such sale or exchange shall be made if there shall be an existing default under the Refunding Mortgage or the General Mortgage or under any mortgage or other indenture executed by the Denver Company to secure bonds or obligations issued to pay or refund the Refunding Bonds or the General Mortgage Bonds, or any of them, which would entitle the trustee under such mortgage or other indenture to foreclose or enforce the same, and every request for any such sale or exchange shall state that no such default is then existing.

In no event shall the Trustee, or any purchaser hereunder of the Utah Fuel Stock, be required to see to the application of the cash proceeds of any such sale by the Denver Company.

Seventh: Upon the written demand of the Denver Company, its successors or assigns, or of the Missouri Pacific and the Western Pacific, jointly, or their successors or assigns, respectively, and upon being furnished with $6,000,000 in cash or $6,000,000 principal amount of the First Consolidated Mortgage 4% Fifty Year Gold Bonds, issued under the Consolidated Mortgage, with all unmatured coupons attached, the Trustee will, if he lawfully may, exer- [fol. 1512] cise the right of withdrawal of the Utah Fuel Stock granted by the Pledge Agreement. In that event, or in the event that at any time in any manner the Trustee shall become vested with title to the Utah Fuel Stock free from the lien or charge of the Consolidated Mortgage, said stock shall remain subject hereto and/or be dealt with in all respects as herein provided with respect to the interest in said stock hereby assigned to the Trustee. Until such event or until the Trustee shall in any manner become vested with title to the Utah Fuel Stock free from the line or charge of the Consolidated Mortgage, the Trustee shall be under no obligation to secure the possession of the certificates for said Utah Fuel Stock or to have the same registered in his name as Trustee hereunder and shall have no responsibility for the custody or safekeeping thereof.

Eighth: The Trustee accepts the trusts of this agreement and agrees to execute them upon the following terms and conditions to which the parties hereto agree:

(a) the Trustee shall be entitled to reasonable compensation for all services rendered by him in the execution of the trusts hereby created and such compensation as well as all reasonable expenses necessarily incurred and actually paid hereunder, together with interest thereon at the rate of six per cent. per annum, the Western Pacific and the Missouri Pacific jointly agree to pay promptly, in equal shares, from time to time as such services are rendered and as such expenses are incurred;

(b) the Trustee may employ agents or attorneys in fact and shall not be answerable for the default or misconduct of any agent or attorney appointed by him in pursuance hereof if such agent or attorney shall have been selected with reasonable care, and the Trustee shall not be responsible for anything whatever in con-

[fol. 1513] nection with this trust except his owa wilful misconduct or gross negligence;

(c) the Trustee may advise with legal counsel and shall be fully protected in respect of any action under this agreement taken or suffered in good faith by him in accordance with the opinion of counsel;

(d) the Trustee shall be protected in acting upon any notice, request, consent, certificate, demand or other paper, document or record believed by him to have been signed by the proper party or parties or to have been properly made;

(e) as to any question of fact necessary to be determined by the Trustee under the provisions hereof, and for the determination of which the method of evidence or proof is not specifically provided, the Trustee may rely upon a written certificate signed by the President or a Vice-President and by the General Auditor or Treasurer of the Denver Company, but the Trustee may make independent investigation should he so determine;

(f) the Trustee shall not be under any obligation to take any action toward the execution or enforcement of the trusts hereby created or to take action under this agreement, which in his opinion, will be likely to involve him in any expense or liability, unless one or more of the parties to this agreement shall, as often as required by the Trustee, furnish him reasonable security and indemnity against such expense or liability;

(g) the parties hereto shall be jointly and severally liable to reimburse and indemnify the Trustee for and against any liability or damage he may sustain or in-[fol. 1514] cur in the execution of this trust, and to reimburse and indemnify the Trustee for and against any liability or responsibility imposed upon him by law or otherwise as a stockholder of Utah Fuel Company.

Ninth: The Trustee may resign and be discharged from the trusts created by this agreement by giving to the Western Pacific, the Denver Company and the Missouri Pacific notice in writing of such resignation, specifying a date when such resignation shall take effect. The Trustee or

any successor hereunder may be removed at any time by an instrument in writing, executed by the Western Pacific, the Denver Company and the Missouri Pacific. In the event of the resignation, removal, death or disability of the Trustee, or any successor, a successor trustee or trustees shall be selected by resolution adopted by the affirmative vote of two-thirds of the entire authorized membership of the Board of Directors of the Denver Company. Any successor trustee may be either an individual or a corporation. Every successor trustee appointed hereunder shall execute and deliver to the Western Pacific, the Denver Company and the Missouri Pacific an instrument accepting such appointment.

Tenth: This agreement, other than the provisions of Articles Second, Third, Fourth, Fifth, Sixth and Eighth hereof, and of this Article Tenth, may at any time be amended by instrument in writing executed by the Denver Company, the Missouri Pacific and the Western Pacific. In case at any time on or after February 1, 1929, no General Mortgage Bonds or Refunding Bonds or bonds or obligations issued to pay or refund the General Mortgage Bonds or the Refunding Bonds, or any of them, shall be outstanding, this agreement shall terminate upon delivery to the Trustee [fol. 1515] of an instrument in writing executed by the Missouri Pacific or by the Western Pacific declaring such termination. Upon the termination of this agreement the Utah Fuel Stock or the interest therein then subject hereto and/or any securities or other property then subject hereto shall vest in equal shares in the Missouri Pacific and the Western Pacific.

Eleventh: The rights and interests of the Denver Company under this agreement may be pledged or assigned under the Refunding Mortgage and/or the General Mortgage and/or any mortgage or other indenture executed by the Denver Company to secure bonds or obligations issued to pay or refund the Refunding Bonds or the General Mortgage Bonds or any of them, but no such pledge or assignment shall prevent the amendment or termination of this agreement as authorized by the provisions of Article Tenth hereof, or any other action authorized by this agreement.

In the event that the rights and interests of the Denver Company hereunder shall be so pledged or assigned under

any such mortgage or other indenture, the trustee thereunder, as long as this agreement and such pledge or assignment shall remain in effect, may enforce by suit or otherwise any and all of the rights of the Denver Company hereunder. So long as this agreement shall remain in effect and any of the preferred stock of the Denver Company shall remain outstanding, any and all of the rights of the Denver Company hereunder may be enforced, by suit or otherwise, by the Preferred Stockholders Committee.

Except as herein otherwise expressly provided, all rights under this agreement may be enforced only by the parties hereto and their respective successors and assigns.

Twelfth: Subject to the provisions of Article Tenth hereof, this agreement shall remain in force so long as [fol. 1516] the Trustee shall hold hereunder any interest in the Utah Fuel Stock or any property received in exchange therefor or any proceeds of any disposition of such interest or of such stock or of any such property. Upon the termination of this agreement pursuant to Article Tenth hereof, the Trustee shall deliver or transfer all interests, property and/or moneys then held by the Trustee hereunder as in such case provided herein or as may be provided in the instrument effecting such termination.

Thirteenth: For all the purposes of this agreement, the ownership of shares of the preferred stock of the Denver Company shall be evidenced by the stock ledgers of the Denver Company. The Trustee may accept as authentic any request, approval or other instrument purporting to be executed by any owner or owners of preferred stock if the execution thereof is duly acknowledged before any official authorized to take acknowledgments of deeds of real estate for record in the State of New York.

Fourteenth: The Western Pacific, the Missouri Pacific and the Denver Company will notify The Guaranty Trust Company of New York, as Trustee under the Consolidated Mortgage, of the execution of this agreement and the rights of the Trustee in the premises hereunder.

Fifteenth: The term "the Trustee" wherever used herein shall, unless the context otherwise requires, be deemed to mean and to include the trustee or trustees for the time being, whether original or successor. The terms "the Missouri Pacific," "the Western Pacific" and "the Denver

Company" wherever used herein shall, unless the context shall otherwise require, be deemed to mean and to include, respectively, Missouri Pacific Railroad Company, The Western Pacific Railroad Corporation and The Denver and Rio Grande Western Railroad Company, and the successors and assigns of said respective corporations. Guar- [fol. 1517] anty Trust Company of New York, when referred to herein, shall be deemed to mean that corporation and/or any person or persons, corporation or corporations, at the time in question its successor or successors as trustee under the Consolidated Mortgage. The terms "preferred stock" or "preferred stock of the Denver Company" wherever used herein, shall be deemed to refer to the preferred stock of the Denver Company authorized at the date of this agreement, and shall not be deemed to refer to or include any preferred stock thereafter authorized.

In Witness Whereof, the parties hereto, other than the Trustee, have caused this instrument to be executed in their respective corporate names and their respective corporate seals to be hereto attached and attested by their respective secretaries or Assistant Secretaries, and the Trustee, in token of his acceptance of the trusts hereby created, has executed this instrument under seal, all as of the day and year first above written.

The Western Pacific Railroad Corporation, by A. R. Baldwin, President. (Seal.)

Attest: S. C. Matthews, Assistant Secretary.
In the presence of: Carl Taylor.

[fol. 1518] The Denver and Rio Grande Western Railroad Company, by Donald C. Swatland, Vice-President. (Seal.)

Attest: John J. McCloy, Assistant Secretary.
In the presence of: Carl Taylor.

Missouri Pacific Railroad Company, by William H. Williams, Chairman of the Board. (Seal.)

Attest: H. L. Utter, Secretary.
In the presence of: Albert Segren.

J. S. Alexander (L. S.)

In the presence of: C. Alison Scully.

[fol. 1519] EXHIBIT 36

Witness Wm. Wyer

The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937

Finance Docket No. 11002

Description of Utah Fuel Company and Subsidiaries

October 10, 1936.

[fol. 1520] Utah Fuel Company and Subsidiaries

Corporate History

The Utah Fuel Company was originally known as Utah Coal & Coke Company, and was incorporated October 20, 1900, under the laws of New Jersey for the objects, among others, of purchasing, leasing or otherwise acquiring coal mines or rights, coal lands or other lands convenient to the business of the company in the State of Utah or elsewhere. There are now outstanding 100,000 shares of capital stock, of no par value, all of which is pledged under the First Consolidated Mortgage of the Rio Grande Western Railway Company by Indenture dated May 23, 1901. It is subject to withdrawal from the lien of the mortgage upon payment of $6,000,000 in cash or upon the deposit with the mortgage trustee of $6,000,000 principal amount of Consolidated Mortgage bonds. On June 20, 1918, the equity in the stock owned by The Denver and Rio Grande Railroad Company was sold under a decree, the title eventually passing to The Western Pacific Railroad Company, which sold a half interest in it to the Missouri Pacific Railroad Company by agreement dated December 20, 1924, which agreement further provided in part that dividends on the Utah Fuel stock were to be distributed as follows:

(a) Dividends declared and paid prior to February 1, 1929, were to be paid to The Denver and Rio Grande Western Railroad Company.

(b) After February 1, 1929, and so long as any Refunding and Improvement or General Mortgage bonds

of The Denver and Rio Grande Western Railroad Company, or any bonds issued to refund them, are outstanding, dividends are to be paid to The Denver and Rio Grande Western Railroad Company, with one exception. If there are no arrears on The Denver and Rio Grande Western Railroad Company Preferred Stock, and moneys are available from net earnings plus the Utah Fuel dividend, and have been appropriated by The Denver and Rio Grande Western Railroad Company for dividends upon the Preferred Stock for a succeeding period of at least 12 months, and such dividends have been declared, then the Utah Fuel dividends in excess of the amount required to provide for the Preferred Stock dividends are payable to the Western Pacific and the Missouri Pacific in equal shares.

(c) If at any time no Refunding and Improvement or General Mortgage bonds, or bonds issued to refund them, are outstanding, dividends are to be paid to the Western Pacific and Missouri Pacific in equal shares.

[fol. 1521] Description of Property

The property of the Utah Fuel Company is valued on its consolidated balance sheet as of December 31, 1935, (see Exhibit B, attached) at $15,118,543, less reserves of $3,149,875. Its holdings of coal lands and surface rights at the present time are as follows:

Coal Rights Field	Acres	Recoverable Coal in Tons (60% Recovery)	Number Mines Operating	Daily Capacity (Tons)
(Utah)				
Carbon Emery	31,413	80,000,000	2	4,700
Castle Gate			1	
Sunnyside			1	
Clear Creek			1	1,200
Somerset	3,699	30,000,000		
(Colorado)				
Walsenburg	4,240	2,000,000	1	700
Total	39,313	112,000,000	6	6,600
Surface Rights only—Utah				
Utah Fuel Co.	8,203			
Utah Grazing Lands Co.	37,163			

At the rate of production obtaining in 1935 (731,391 tons), potential coal reserves will last 153 years.

The Castle Gate mines are by far the most important, both in actual and potential production. Equipment is

modern and powered by electricity; the steel tipple completed about 1928 is as efficient an installation as any in the United States.

The Clear Creek mine is old, but there are still available some 6,000,000 tons which can be produced at a reasonable cost, and equipment is fairly efficient.

The Sunnyside property contains a large amount of fairly good coal, although it is not suitable for domestic use. About 1930 natural gas was piped into Ogden and Salt Lake from the Wyoming fields, thus cutting off the market for about 40,000 tons of Sunnyside coal annually which had formerly been used for the manufacture of gas. A substantial proportion of the production in this field has been used in the past for the manufacture of coke in bee-hive ovens, but the bulk of this market has been lost to cheaper coke manufactured in modern by-product plants.

[fol. 1522] The Somerset mine contains a good quality of coal in large amounts, but its production depends almost entirely upon demand from the Denver and Rio Grande Western.

Calumet Mine No. 1 at Walsenburg has been exhausted. Mine No. 2 contains good coal in substantial amounts.

Financial Situation

A summarized comparative income account for the years 1930-1935, inclusive, is attached as Exhibit A. A consolidated balance sheet as of December 31, 1935, is attached as Exhibit B. The subsidiary companies included on this balance sheet are engaged in the following activities:

Calumet Fuel Company owns the mines at Walsenburg.

Wasatch Store Company sells supplies to the miners. There is a store at each mine. In 1935 gross sales of $258,435 resulted in net income of $8,229.

Utah Fuel Stoker Sales Company markets stokers made by the Link-Belt Company of Chicago. In 1935, 143 stokers were sold, yielding gross of $29,361. Operations for the year resulted in a loss of $476.

The Bamberger Coal Company, at Salt Lake, and the Utah Fuel-Coal Company at San Francisco, are selling organizations.

The Utah Grazing Lands Company owns land which at present is used only for grazing, and its income is derived

entirely from rentals which amounted to $4,332 in 1935. After charges there was a deficit of $295.

The greatest problem of the Utah Fuel Company is the fact that it is burdened with coal lands far in excess of its needs for many years to come, as is indicated in the summary of coal lands owned shown above. In recent years competition from Wyoming natural gas, fuel oil shipped into Salt Lake and Ogden from California, and more agressive selling by its Utah coal competitors, has served not only to reduce its total sales, but also its proportionate share of the coal marketed in Utah and Colorado. Its coke business will never be regained as coke manufactured in bee-hive ovens cannot compete with modern by-product plants which are now supplying the Salt Lake smelters, and the Utah Fuel Company did not seize its opportunity a few years ago to acquire such a plant itself. The two railroads which own the stock have themselves been forced to distribute some of their coal orders to competitors of the Utah Fuel in order to obtain reciprocal business.

The first seven months of 1936 show a marked improvement over 1935. In that period, 422,046 tons of coal and 7,097 tons of coke were sold, as compared with 363,182 tons and 3,438 tons respectively last year. Dollar sales of $902,621 compare with $733,574 in 1935.

(Here follow 2 photolithographs, side folios 1523, 1524)

UTAH FUEL COMPANY AND SUBSIDIARY COMPANIES

Exhibit A

Summaries of Consolidated Income, Years Ended December 31, 1930 to 1935, inclusive

	1930	1931	1932	1933	1934	1935
Gross Earnings from Sale of Coal, Coke and Merchandise	$2,617,804.82	$1,742,998.09	$1,306,741.99	$1,295,507.27	$1,416,869.55	$1,650,286.93
Net Earnings from Rentals, etc.	53,449.90	62,501.46	56,083.92	53,260.89	52,282.53	48,691.48
Net Income from Other Sources - Interest, etc.	40,891.54	6,631.53	10,141.14	9,440.71	7,941.12	12,370.24
Total Income	$2,712,146.26	$1,812,131.08	$1,373,967.05	$1,358,208.87	$1,477,093.20	$1,711,348.65
Operating Expenses	$2,072,418.81	$1,372,578.59	$1,011,654.88	$ 979,382.33	$1,097,727.40	$1,303,147.58
Income Charges	657,161.65	572,336.61	521,189.89	477,880.19	425,492.11	405,210.04
Total Cost	$2,729,580.46	$1,944,915.20	$1,532,844.77	$1,457,262.52	$1,523,219.51	$1,708,357.62
Total Net Income	$D 17,434.20	$D 132,784.12	$D 159,877.72	$D 99,053.65	$D 48,126.31	$D 2,991.03
Income Charges include for all mines and ovens -						
Depletion of Coal Lands	$ 16,620.	$ 14,689.	$ 13,255.	$ 14,765.	$ 15,002.	$ 15,884.
Depreciation and Amortization of Property	260,049.	254,698.	250,807.	224,822.	169,679.	160,872.

Note: D - Deficit.

1523

Exhibit B

UTAH FUEL COMPANY AND SUBSIDIARY COMPANIES

Consolidated Balance Sheet as of December 31, 1935 and 1934

	UTAH FUEL COMPANY	The Calumet Fuel Company	Wasatch Store Company	Utah Fuel Stoker Sales Company	Bamberger Coal Company	Utah Fuel-Coal Company	Utah Grazing Lands Company	Eliminations	1935	1934	I
A S S E T S											
Cash	$ 113,823	$ 61,764	$ 75,840	$ 947	$ 175	$ 1,842	$	$	$ 252,391	$ 40,759	$
Accounts Receivable:											
Railroads	57,797	3,509							61,305	231,740	
All Others	167,633	13,009	29,900	1,019	33,119	5,151	350		250,180	213,858	
Affiliated Companies	65,850		5,500					71,350			
Bills Receivable	6,047	1,700	525	4,275					12,547	15,513	
Inventories - Coal, Coke, Supplies and Merchandise	117,631	12,781	42,134	10,628	22,525	9,251			214,950	205,800	
Securities Owned:											
Guaranty Fund - U. S. Bonds Deposited in accordance with Colorado Workmen's Compensation Act	34,788	53,454							88,242	88,242	
Stocks of Subsidiary Companies (Par Value)	873,500		8,360					881,660	-	8,360	
Deferred Debit Items	2,345	2,450	100		166				5,062	8,724	
Cash Surrender Value of Insurance on Life of A. B. Apperson		9,448							9,448	8,009	
Property	13,935,364	1,052,169	67,690	259	24,087	974	38,000		15,118,543	15,256,382	
T O T A L	$15,374,778	$1,210,285	$228,048	$17,128	$80,072	$17,218	$38,350	$953,210	$16,012,668	$16,087,387	
L I A B I L I T I E S											
Accounts Payable:											
Pay Rolls, Vouchers, etc.	$ 103,152	$ 16,466	$ 19,433	$ 4,592	$ 2,705	$ 116	$	$	$ 146,464	$ 167,175	
Provision for Federal Income Tax	1,082		1,469						2,552	220	
Affiliated Companies				5,500	38,560	6,369	922	71,350			
Deferred Credit Items	250								250	250	
Accrued Expenses	14,208	9,248	711	67	320	61			24,615	23,840	
Reserves	2,638,750	461,961	39,630	374	8,486	672			3,149,875	3,205,167	
CAPITAL STOCK	10,000,000	665,500	150,000	8,360	10,000	10,000	38,000	881,860	10,000,000	10,000,000	
Excess of Par Value over Cost of Stock of Subsidiary Companies	43,599								43,599	43,599	
Unrealized Profit				1,166					1,166		

Exhibit B

1934					
ah -Coal pany	Utah Grazing Lands Company	Eliminations	1935	1934	Increase
,842	$	$	$ 252,391	$ 40,759	$211,632
			61,305	231,740	170,434 D
,151	350		250,180	213,858	36,322
		71,350			
			12,547	15,513	2,966 D
,251			214,950	205,800	9,149
			88,242	88,242	
		881,860	-	8,360	8,360 D
			5,062	8,724	3,663 D
			9,448	8,009	1,438
974	38,000		15,118,543	15,266,382	147,838 D
,218	$38,350	$953,210	$16,012,668	$16,087,387	$ 74,719 D
116	$	$	$ 146,464	$ 167,175	$ 20,711 D
			2,552	220	2,332
,369	922	71,350			
			250	250	
61			24,615	23,840	775
672			3,149,875	3,205,167	55,292 D
,000	38,000	881,860	10,000,000	10,000,000	

Consolidated Balance Sheet as of December 31, 1935 and 1934

	UTAH FUEL COMPANY	The Calumet Fuel Company	Wasatch Store Company	Utah Fuel Stoker Sales Company	Bamberger Coal Company	Utah Fuel-Coal Company	Utah Grazing Lands Company	Eliminations	19
ASSETS									
Cash	$ 113,823	$ 61,764	$ 73,840	$ 947	$ 175	$ 1,842	$	$	$ 25
Accounts Receivable:									
Railroads	57,797	3,509							6
All Others	167,633	13,009	29,900	1,019	33,119	5,151	350		25
Affiliated Companies	65,850		5,500					71,350	
Bills Receivable	6,047	1,700	525	4,275					1
Inventories - Coal, Coke, Supplies and Merchandise	117,631	12,781	42,134	10,628	22,525	9,251			21
Securities Owned:									
Guaranty Fund - U. S. Bonds Deposited in accordance with Colorado Workmen's Compensation Act	34,788	53,454							
Stocks of Subsidiary Companies (Par Value)	873,500		8,360					881,860	8
Deferred Debit Items	2,345	2,450	100		166				
Cash Surrender Value of Insurance on Life of A. B. Apperson		9,448							
Property	13,935,364	1,052,169	67,690	259	24,087	974	38,000		15,11
TOTAL	$15,374,778	$1,210,285	$228,048	$17,128	$80,072	$17,218	$38,350	$953,210	$16,01
LIABILITIES									
Accounts Payable:									
Pay Rolls, Vouchers, etc.	$ 103,152	$ 16,466	$ 19,433	$ 4,592	$ 2,705	$ 116	$	$	$ 14
Provision for Federal Income Tax	1,082		1,469						
Affiliated Companies				5,500	58,560	6,369	922	71,350	
Deferred Credit Items	250								
Accrued Expenses	14,208	9,248	711	67	320	61			2
Reserves	2,638,750	461,961	39,630	374	8,486	672			3,14
CAPITAL STOCK	10,000,000	665,500	150,000	8,360	10,000	10,000	38,000	881,860	10,00
Excess of Par Value over Cost of Stock of Subsidiary Companies	43,599								
Unrealized Profit				1,166					4
SURPLUS	2,573,736	57,109	16,805	D 2,931	-	-	D 572		2,64
TOTAL	$15,374,778	$1,210,285	$228,048	$17,128	$80,072	$17,218	$38,350	$953,210	$16,01

Note: D - Decrease or Deficit.

ah -Coal pany	Utah Grazing Lands Company	Eliminations	1935	1934	Increase
,842	$	$	$ 252,391	$ 40,759	$211,632
			61,305	231,740	170,434 D
,151	350		250,180	213,858	36,322
		71,350			
			12,547	15,513	2,966 D
,251			214,950	205,800	9,149
			88,242	88,242	
		881,860	-	8,360	8,360 D
			5,062	8,724	3,663 D
			9,448	8,009	1,438
974	38,000		15,118,543	15,266,382	147,838 D
,218	$38,350	$953,210	$16,012,668	$16,087,387	$ 74,719 D
116	$	$	$ 146,464	$ 167,175	$ 20,711 D
			2,552	220	2,332
,369	922	71,350			
			250	250	
61			24,615	23,840	775
672			3,149,875	3,205,167	55,292 D
,000	38,000	881,860	10,000,000	10,000,000	
			43,599	43,599	
			1,166		1,166
-	D 572		2,644,147	2,647,136	2,989 D
,218	$38,350	$953,210	$16,012,668	$16,087,387	$ 74,719 D

[fol. 1525]

EXHIBIT 37a

Witness Wm. Wyer

The Denver and Rio Grande Western System Proposed Plan of Consolidation and Reorganization as of January 1, 1937

Finance Docket No. 11002

This assignment made and delivered this 20th day of December, one thousand nine hundred and twenty-four, by The Denver and Rio Grande Western Railroad Company, a Delaware corporation (hereinafter called the Railroad Company), to and in favor of The Equitable Trust Company of New York, a New York corporation, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company, dated February 1, 1924 (hereinafter called the Refunding Mortgage Trustee), and, subject to the rights of the Refunding Mortgage Trustee, to The Farmers' Loan and Trust Company, as Trustee under the General Mortgage of The Denver and Rio Grande Western Railroad Company, dated February 1, 1924 (hereinafter called the General Mortgage Trustee).

Witnesseth that in consideration of the sum of ten dollars ($10.00), lawful money, and other good and valuable consideration, the receipt whereof is hereby acknowledged, the Railroad Company has sold, assigned, transferred and set over and does hereby sell, assign, transfer and set over unto the Refunding Mortgage Trustee, its successors and assigns, upon the trusts set forth in said Refunding and Improvement Mortgage, and, subject thereto, to the General Mortgage Trustee upon the trusts set forth in said General Mortgage, all rights and interests of the Railroad Company in, to and under the attached agreement relating to the stock of Utah Fuel Company, between The Western Pacific Railroad Corporation, The Denver and Rio Grande Western Railroad Company, Missouri Pacific Railroad Company and James S. Alexander, as Trustees, dated December 20, 1924; provided, however, that nothing in this assignment contained shall entitle either of such Trustees to any dividends payable and/or paid to the Railroad Company under Article Second of said agreement or shall pre-

[fol. 1526] vent the exercise by the Railroad Company of

the right to consent to or take or request the taking of any action authorized by said agreement.

In Witness Whereof The Denver and Rio Grande Western Railroad Company has caused this instrument to be signed in its name by its President or a Vice-President, and its corporate seal to be hereunto affixed, and to be attested by its Secretary or an Assistant Secretary, the day and year first above written.

The Denver and Rio Grande Western Railroad Company, by Donald C. Swatland, Vice-President. (Seal.)

Attest: John J McCloy, Assistant Secretary.

Copy of original document, September 16, 1936.

[fol. 1527] EXHIBIT 69

Segregation Formula Before Re ision

Utah Fuel Company Stock

The RGW Consolidated Mortgage is a first lien on all of the capital stock of the Utah Fuel Company, a detailed description of which is furnished as a separate exhibit. No dividends were paid during the year ended June 30, 1935, but $250,000 was paid in the six months ended June 30, 1934, just prior to the period included in the income account under discussion. This was the first dividend for several years, and was paid from funds accumulated through depletion of coal lands, rather than from earnings.

In determining a proper allowance to make the RGW Consols for this stock, neither the earnings of the company in the past, nor the book value of its property at the moment, furnish a suitable base. It was finally decided to allow ⅓ of the $250,000 dividend received in 1934, or $83,333, as a fair sum for the purpose of calculating the relative earnings of the various mortgage districts.

(Here follows 1 photolithograph, side folio 1528)

THE DENVER AND RIO GRANDE WESTERN SYSTEM
Proposed Plan of Consolidation and Reorganization as of January 1, 1937
Finance Docket No. 11002

Operating Revenues, Operating Expenses by General Accounts and Ratios
Maintenance Expenses incurred in connection with Additions and Betterments w
1925 to 1936 inclusive, and estimate for Normal Year

	Normal Year		1936		1935		1934		1933		1932		1931		
D&RGW (Includes D&SLW - RGVet and GV) Gross Ton Miles Excluding Locomotives and Tenders, but Including Company Freight (000)	(1)6,966,792		6,076,599		4,755,186		4,617,602		4,102,421		3,903,183		4,682,619		5,
Net Ton Miles Revenue Freight (000)	(1)2,563,173		(2)2,199,828		1,722,027		1,611,357		1,446,569		1,335,840		1,672,944		2,
	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	A
Gross Revenues	$30,734,000	100.0%	$25,599,309	100.0%	$20,944,230	100.0%	$19,246,850	100.0%	$17,112,794	100.0%	$17,340,621	100.0%	$23,484,818	100.0%	$29,
Maintenance of Way and Structures	3,995,420	13.0	4,015,100	15.7	2,491,669	11.9	2,259,308	11.7	1,640,960	9.6	1,822,743	10.4	2,703,660	11.5	3,
Maintenance of Equipment	6,146,800	20.0	6,503,865	25.4	4,861,413	23.2	4,309,191	22.4	3,460,148	20.2	3,619,224	20.6	4,485,324	19.1	5,
Total Maintenance	10,142,220	33.0	10,518,965	41.1	7,353,082	35.1	6,568,499	34.1	5,101,108	29.8	5,441,967	31.0	7,188,984	30.6	9,
Traffic	768,350	2.5	659,247	2.5	601,383	2.9	552,992	2.9	519,978	3.0	556,850	3.2	641,171	2.7	
Transportation	10,065,385	32.7	8,800,742	34.4	7,140,624	34.2	6,364,088	33.1	5,366,292	31.4	5,690,025	32.4	7,387,345	31.4	9,
Miscellaneous	230,505	.7	182,735	.7	127,227	.6	86,072	.5	57,572	.3	103,418	.6	199,088	.8	
General	1,106,424	3.6	1,012,407	4.0	963,815	4.6	1,098,593	5.7	857,173	5.0	927,948	5.3	1,034,368	4.4	1,
Transportation for Investment - Cr.	92,202	.3	235,137	.9	50,663	.2	25,183	.1	14,699	.1	9,699	.1	27,716	.1	
Total Operating Expenses	22,220,682	72.3	20,938,959	81.8	16,135,468	77.2	14,645,261	76.2	11,887,424	69.4	12,710,507	72.4	16,423,440	69.8	20,
Maintenance Expenses Incurred in Connection with Additions and Betterments Program	(3) 307,340	1.0	(4) 652,000	2.5	232,178	1.1	253,299	1.3	48,203	.3	73,703	.4	330,418	1.4	
Maintenance Expenses After Deducting Expenses Incurred in Connection with Additions and Betterments Program	9,834,880	32.0	9,866,965	38.5	7,120,904	34.0	6,315,400	32.8	5,052,905	29.5	5,368,264	30.6	6,858,566	29.2	8,
Total Operating Expenses After Deducting Expenses Incurred in Connection with Additions and Betterments Program	21,913,341	71.3	20,286,959	79.3	15,903,290	76.1	14,391,962	74.9	11,839,221	69.1	12,636,804	72.0	16,093,022	68.4	20,
D&SL Ry															
Gross Revenues	2,987,189	100.0	(5)2,840,685	100.0	2,234,861	100.0	1,820,006	100.0	1,657,331	100.0	1,915,469	100.0	2,302,835	100.0	3,
Maintenance of Way and Structures	350,000	11.7	455,765	16.0	261,026	11.7	93,942	5.8	214,820	13.0	246,893	12.9	358,080	15.5	
Maintenance of Equipment	568,000	19.0	712,120	25.1	423,916	19.1	251,474	15.5	276,358	16.7	294,125	15.4	395,308	17.2	
Traffic	20,000	.7	27,885	1.0	23,127	1.0	18,474	1.1	18,193	1.1	20,150	1.0	23,161	1.0	
Transportation	717,600	24.0	723,261	25.5	514,719	23.0	332,965	20.6	301,981	18.2	321,236	16.7	395,597	17.2	
Miscellaneous	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
General	50,000	1.7	116,332	4.1	116,482	5.2	134,365	8.2	120,152	7.2	116,464	6.1	131,228	5.7	
Transportation for Investment - Cr.	8,000	.3	77,432	2.7	62,589	2.8	16,369	1.0	42,343	2.5	19,171	1.0	-	-	
Total Operating Expenses	1,697,600	56.8	1,957,930	68.9	1,276,681	57.1	814,851	50.2	889,160	53.7	979,699	51.1	1,303,369	56.6	1

HE DENVER AND RIO GRANDE WESTERN SYSTEM
Consolidation and Reorganization as of January 1, 1937
Finance Docket No. 11002

Exhibit 17
Witness Hoyt

use, Operating Expenses by General Accounts and Ratios
incurred in connection with Additions and Betterments work
1936 inclusive, and estimate for Normal Year

33	1932		1931		1930		1929		1928		1927		1926		1925	
	3,903,183 1,335,840		4,682,819 1,672,944		5,556,238 2,057,444		5,652,079 2,250,518		5,291,893 2,082,207		5,104,996 2,036,281		4,923,761 1,944,114		4,518,532 1,854,855	
Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue	Amount	Percent of Gross Revenue
100.0%	$17,540,431	100.0%	$23,484,818	100.0%	$29,747,537	100.0%	$34,828,669	100.0%	$33,200,656	100.0%	$33,121,169	100.0%	$34,030,309	100.0%	$33,629,463	100.0%
9.6	1,822,743	10.4	2,703,860	11.5	3,862,180	13.0	5,441,659	15.6	6,178,490	18.6	6,748,481	20.4	5,899,285	17.3	5,742,197	17.0
20.2	3,619,224	20.6	4,485,224	19.1	5,577,686	18.7	6,592,013	18.9	6,164,141	18.6	6,106,950	18.4	6,242,158	18.3	5,948,303	17.6
29.8	5,441,967	31.0	7,188,984	30.6	9,439,866	31.7	12,033,673	34.5	12,342,571	37.2	12,855,431	38.8	12,141,423	35.6	11,690,500	34.6
3.0	536,850	3.2	641,171	2.7	727,410	2.5	751,492	2.1	702,899	2.1	687,957	2.1	675,673	2.0	652,277	1.9
31.4	5,490,025	32.4	7,387,345	31.4	9,179,737	30.8	10,236,514	29.3	10,003,469	30.2	10,079,155	30.4	10,304,180	30.3	10,835,670	32.3
.3	103,418	.6	199,088	.8	340,204	1.2	499,665	1.4	474,035	1.4	535,486	1.6	561,835	1.7	623,420	1.9
5.0	927,946	5.3	1,034,568	4.4	1,091,383	3.7	1,098,634	3.1	1,047,754	3.1	1,050,682	3.1	1,051,033	3.1	1,042,650	3.1
.1	9,699	.1	27,716	.1	84,799	.3	84,811	.2	128,313	.4	129,495	.4	119,630	.4	50,269	.2
69.4	12,710,507	72.4	16,423,440	69.8	20,693,801	69.6	24,535,166	70.2	24,442,415	73.6	25,079,216	75.6	24,614,314	72.3	24,796,249	73.6
.3	73,703	.4	330,415	1.4	562,601	1.9	1,304,297	3.7	1,760,932	5.3	2,154,254	6.5	1,350,883	4.0	983,145	2.9
29.5	5,368,264	30.6	6,858,566	29.2	8,877,265	29.8	10,729,376	30.8	10,581,639	31.9	10,701,177	32.3	10,790,540	31.6	10,707,355	31.7
69.1	12,636,804	72.0	16,083,022	68.4	20,131,200	67.7	23,230,869	76.5	22,681,483	68.3	22,924,962	69.1	23,263,431	68.3	23,811,104	70.7
100.0	1,915,469	100.0	2,302,835	100.0	3,197,281	100.0	3,981,131	100.0	4,011,663	100.0	4,110,286	100.0	4,268,447	100.0	3,889,321	100.0
13.0	246,893	12.9	358,080	15.5	626,161	19.6	660,393	16.6	824,448	20.8	1,108,933	27.0	1,289,899	30.3	875,946	22.5
16.7	294,125	15.4	395,303	17.8	641,779	20.1	785,256	19.7	902,749	22.5	1,217,467	29.6	1,323,389	31.0	1,120,855	28.9
1.1	20,150	1.0	23,161	1.0	26,836	1.0	26,703	.7	22,995	.6	21,636	.5	21,318	.5	18,382	.5
18.2	321,236	16.7	395,597	17.2	513,896	16.1	610,268	15.3	687,738	17.1	919,422	22.3	999,830	23.5	1,027,757	26.4
-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
7.2	116,466	6.1	131,228	5.7	180,937	5.6	163,993	4.1	129,486	3.2	122,320	3.0	114,953	2.7	78,398	2.0
2.5	19,171	1.0	-	-	14,651	.5	19,966	.5	31,094	.8	14,276	.3	22,988	.5	-	-
53.7	979,699	51.1	1,303,369	56.6	1,974,951	61.9	2,226,647	55.9	2,536,322	63.2	3,375,502	82.1	3,725,901	87.5	3,121,338	80.3

Betterments Program	9,834,880	32.0	9,000,905	30.9	7,440,904	34.0	6,313,400	32.8	5,052,905	29.9	5,000,804	30.0	5,000,000	31.6	6,000,000
Total Operating Expenses After Deducting Expenses Incurred in Connection with Additions and Betterments Program	21,913,341	71.3	20,886,959	79.3	15,838,290	76.1	14,391,962	74.9	11,839,221	69.1	12,636,804	72.0	16,093,022	68.4	20,131,200
D&SL Ry															
Gross Revenues	2,987,189	100.0	(5)3,840,685	100.0	2,234,881	100.0	1,820,006	100.0	1,657,331	100.0	1,915,469	100.0	2,302,835	100.0	3,197,282
Maintenance of Way and Structures	350,000	11.7	455,765	16.0	261,026	11.7	93,942	5.8	214,820	13.0	246,893	12.9	358,080	15.5	626,161
Maintenance of Equipment	568,000	19.0	712,120	25.1	423,916	19.1	251,474	15.5	276,358	16.7	294,125	15.4	395,303	17.2	641,779
Traffic	20,000	.7	27,885	1.0	23,127	1.0	18,474	1.1	18,192	1.1	20,150	1.0	23,161	1.0	26,836
Transportation	717,600	24.0	723,361	25.5	514,719	23.0	332,965	20.6	301,981	18.2	321,236	16.7	395,597	17.2	513,896
Miscellaneous	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
General	50,000	1.7	116,332	4.1	116,482	5.2	134,365	8.2	120,152	7.2	116,466	6.1	131,228	5.7	180,937
Transportation for Investment - Cr.	8,000	.3	77,432	2.7	62,589	2.8	16,369	1.0	42,343	2.5	19,171	1.0	-	-	14,651
Total Operating Expenses	1,697,600	56.8	1,957,930	68.9	1,276,681	57.1	814,851	50.2	889,160	53.7	979,699	51.1	1,303,369	56.6	1,974,951
System															
Gross Revenues	33,721,189	100.0	28,439,994	100.0	23,179,111	100.0	20,866,856	100.0	18,770,125	100.0	19,476,090	100.0	25,787,652	100.0	32,944,819
Maintenance of Way and Structures	4,345,420	12.85	4,470,865	15.7	2,752,696	11.9	2,353,450	11.3	1,855,780	9.9	2,069,636	10.6	3,061,740	11.9	4,488,341
Maintenance of Equipment	6,714,800	19.91	7,215,985	25.4	5,285,329	22.8	4,560,465	21.9	3,726,508	19.9	3,913,349	20.1	4,880,627	18.9	6,219,465
Traffic	788,350	2.34	687,132	2.4	624,510	2.7	571,456	2.7	538,170	2.9	577,000	3.0	664,332	2.6	754,266
Transportation	10,782,985	31.98	9,524,003	33.5	7,655,343	33.1	6,897,053	32.0	5,668,273	30.2	6,011,261	30.9	7,782,942	30.2	9,693,633
Miscellaneous	230,505	.68	182,735	.6	127,227	.5	86,872	.4	57,572	.3	103,418	.5	199,088	.8	340,204
General	1,156,424	3.43	1,128,739	4.0	1,080,297	4.7	1,232,958	5.9	977,325	5.2	1,044,412	5.4	1,165,796	4.5	1,272,313
Transportation for Investment - Cr.	100,202	.30	312,569	1.1	113,252	.5	41,562	.2	87,042	.3	28,870	.2	27,716	.1	99,450
Total Operating Expenses	23,918,282	71.49	22,896,889	80.5	17,412,149	75.2	15,460,112	74.0	12,776,584	68.1	13,690,206	70.3	17,726,809	68.8	22,668,752

Note 1 - Average haul per ton of revenue freight, twelve months ended November 31, 1936 — 240.0 miles

Tons of revenue freight estimated for normal year -

Carload	10,565,974	
L C L	113,915	10,679,889

Estimated revenue ton miles, normal year (1000's) — 2,563,173

1935 Gross ton miles		4,755,186
Net Ton Miles Revenue Freight		1,722,027
Ton Miles of Cars per Ton Miles of Revenue Freight		1.76138
Average Car Load 1935	31.7 tons	
" " " Normal Year	32.5 "	
" " " Increase over 1935	.8 or 2.523%	
Net Ton Miles Revenue Freight Normal Year		2,563,172
Reduced to amount comparable with 1935 by dividing by 102.523%		2,500,096
Ton Miles of Cars required at 1.76138		4,403,619
Ton Miles Revenue Freight Normal Year		2,563,173
Gross Ton Miles Normal Year		6,966,792

Source - Company Records
Estimate for normal year

February 8, 1937

Note 2 - 1935 - Gross ton miles including company freight (1000's)
Net ton miles exluding company freight (1000's)
Percent gross to net ton miles

1936 - Gross ton miles including company freight (1000's) actual
Net ton miles excluding company freight (estimate, using same ratio to gross as obtained in 1935) (1000's)

Note 3 - Estimated gross revenue, normal year

Estimate for maintenance in connection with Additions and Betterm

Way and Structures	3/4% of gross
Equipment	1/4% of gross
Total	1%

Total estimated maintenance expenses to be incurred in connection
Additions and Betterments work, 1% of gross revenue

	[illegible]	[illegible]	30.6	6,858,566	29.2	8,877,265	29.8	10,729,376	30.8	10,581,639	31.9	10,701,177	32.3	10,790,540	31.6	10,707,355	31.7
	69.1	12,636,804	72.0	16,093,022	68.4	20,131,200	67.7	23,230,869	76.5	22,681,483	68.3	22,924,962	69.1	23,263,431	68.3	23,811,104	70.7
	100.0	1,915,469	100.0	2,302,835	100.0	3,197,282	100.0	3,981,131	100.0	4,011,663	100.0	4,110,286	100.0	4,268,447	100.0	3,889,321	100.0
	13.0	246,893	12.9	358,080	15.5	626,161	19.6	660,393	16.6	824,448	20.6	1,108,932	27.0	1,289,399	30.3	875,946	22.5
	16.7	294,125	15.4	395,303	17.2	641,779	20.1	785,256	19.7	902,749	22.5	1,217,467	29.6	1,323,389	31.0	1,120,855	28.9
	1.1	20,150	1.0	23,161	1.0	26,836	1.0	26,703	.7	22,995	.6	21,636	.5	21,318	.5	18,382	.5
	18.2	321,236	16.7	395,597	17.2	513,896	16.1	610,268	15.3	687,738	17.1	919,422	22.3	999,830	23.5	1,027,757	26.4
	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	7.2	116,446	6.1	131,228	5.7	180,937	5.6	163,993	4.1	129,486	3.2	122,320	3.0	114,953	2.7	78,398	2.0
	2.5	19,171	1.0	-	-	14,651	.5	19,966	.5	31,094	.8	14,276	.3	22,988	.5	-	-
	53.7	979,699	51.1	1,303,369	56.6	1,974,951	61.9	2,226,647	55.9	2,536,322	63.2	3,375,502	82.1	3,725,901	87.5	3,121,338	80.3
	100.0	19,476,090	100.0	25,787,653	100.0	32,944,819	100.0	38,809,800	100.0	37,212,319	100.0	37,231,455	100.0	38,298,756	100.0	37,518,784	100.0
	9.9	2,089,636	10.6	3,061,740	11.9	4,468,341	13.6	6,102,052	15.7	7,002,878	18.8	7,857,414	21.1	7,188,664	18.6	6,618,143	17.6
	19.9	3,913,349	20.1	4,880,627	18.9	6,219,465	18.9	7,377,269	19.0	7,066,890	19.0	7,324,417	19.7	7,565,547	19.7	7,069,158	18.9
	2.9	577,000	3.0	664,332	2.6	756,265	2.3	778,195	2.0	725,894	1.9	709,893	1.9	696,991	1.8	670,659	1.8
	30.2	6,011,261	30.9	7,782,942	30.2	9,693,633	29.4	10,846,782	28.0	10,691,207	28.8	10,998,577	29.4	11,304,010	29.5	11,863,427	31.6
	.3	103,418	.5	199,088	.8	340,204	1.0	499,665	1.3	474,035	1.3	535,486	1.4	561,835	1.5	623,420	1.7
	5.2	1,044,412	5.4	1,165,796	4.5	1,272,313	3.9	1,262,627	3.2	1,177,240	3.1	1,173,002	3.2	1,165,986	3.0	1,121,048	3.0
	.3	28,870	.2	27,716	.1	99,450	.3	104,777	.3	159,407	.4	143 771	.4	142,818	.4	50,269	.1
	68.1	13,690,206	70.3	17,726,809	68.8	22,668,752	68.8	28,761,813	68.9	28,978,737	72.5	28,454,718	76.3	28,340,215	73.7	27,915,587	74.5

935 - Gross ton miles including company freight (1000's) 4,755,186
Net ton miles exeluding company freight (1000's) 1,722,027
Percent gross to net ton miles 276.14%

936 - Gross ton miles including company freight (1000's) actual 6,074,599
Net ton miles excluding company freight (estimate, using same ratio to gross as obtained in 1935) (1000's) 2,199,826

Estimated gross revenue, normal year $30,734,000

Estimate for maintenance in connection with Additions and Betterments work -

Way and Structures	3/4% of gross	
Equipment	1/4% of gross	
Total	1%	1%

Total estimated maintenance expenses to be incurred in connection with Additions and Betterments work, 1% of gross revenue $ 307,340

Note 4 - Estimate, maintenance of way only 588,000
Add 1/4% on estimate for maintenance of equipment 64,000
652,000

Note 5 - December 1936 figures for D&SL are estimated.

[fol. 1529] EXHIBIT 117-a

Witness Pyeatt

The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937

Finance Docket No. 11002

Correction in Exhibit 117

In column headed "Normal Year", following corrections should be made:

Gross Ton Miles Excluding Locomotives and Tenders, but including Company Freight (1000's)	(1)	7,228,028
Net Ton Miles Revenue Freight (1000's)	(1)	2,659,292

Note 1 should be corrected to read as follows:

Note 1. Average haul per ton of revenue freight, eleven months ended November 30, 1936		249.0 miles
Tons of revenue freight estimated for normal year—		
Carload	10,565,974	
Less than Carload	113,915	10,679,889
Estimated revenue ton miles, normal year (1000's)		2,659,292
1935—Gross ton miles, including company freight		4,755,186
Net ton miles, revenue freight		1,722,027
Ton Miles of Cars and Company freight per ton mile of revenue freight		1.76139
Average carload, carload revenue freight only, 1935	31.7 tons	
Average carload, carload revenue freight only, Normal Year	32.5	
	.8 or 2.524%	

[fol. 1534]

The Denver and Salt Lake Railway Company
Estimated Income Account for "Normal Year"

		Normal Year	Per cent of Operating Revenues
Railway Operating Revenues:			
Freight		$2,790,189	93.4
Passenger		90,000	3.0
Mail		65,000	2.2
Express		12,000	.4
Miscellaneous		15,000	.5
Incidental		15,000	.5
Total Railway Operating Revenues		2,987,189	100.0
Railway Operating Expenses:			
Maintenance of Way and Structures		$350,000	11.7
Maintenance of Equipment		565,600	19.0
Traffic		20,000	.7
Transportation		717,600	24.0
General		50,000	1.7
Transportation for Investment—Cr.		8,000	.3
Total Railway Operating Expenses		1,697,600	56.8
Net Revenue from Railway Operations		1,289,589	
Tax Accruals		275,000	
Railway Operating Income		1,014,589	
Equipment Rents—Net Debit		65,000	
Joint Facility Rents—Net Credit		537,950	
Total Rents		472,950	
Net Railway Operating Income		1,487,539	
Non-Operating Income		20,000	
Gross Income		1,507,539	
Miscellaneous Deductions from Gross Income:			
Rent for Leased Road	$404,200		
Miscellaneous Income Charges	10,274	414,474	
Amount Available for Interest		1,093,065	

[fol. 1536]

EXHIBIT 155
Witness Wyu

The Denver and Rio Grande Western System
Proposed Plan of Consolidation and Reorganization as of January 1, 1937
Finance Docket No. 11002

Utah Fuel Company and Subsidiary Companies
Consolidated Income Account—1936
(Supplement to Exhibit 36)

Gross earnings from sale of coal, coke, merchandise, etc.	$1,902,202	
Net earnings from rentals, etc.	48,629	
Net income from other sources, interest, etc.	8,179	
		$1,959,009
Operating Expenses	$1,563,959	
Income Charges	383,988	1,947,947
Net Income (before charging Federal Income Taxes)		$11,062
Provision for Federal Income Taxes		3,509
Net Income (after charging Federal Income Taxes)		$7,553

Corrections in Exhibit A of Exhibit 36:

(1) Total Net Income for years 1934 and 1935 are shown as deficits of $46,126.31 and $2,991.03, respectively. The correct figures are a deficit of $46,346.14 for 1934, and a net income of $439.37 for 1935. The corrected figures are after Federal Income Taxes of $219.83 in 1934; and $2,551.66 in 1935.

(2) The charges for "Depletion of Coal Lands" and "Depreciation and Amortization of Property" for all mines and ovens which are included in "Income Charges" are shown in the lower half of the statement. The figures shown cover the Utah Fuel Company only. Figures for the consolidated income account should include the Calumet Fuel Company also, and the correct figures are shown below:

	Depletion of Coal Lands	Depreciation and Amortization of Property
1930	$20,906	$300,929
1931	17,212	298,568
1932	14,752	295,654
1933	15,586	267,060
1934	16,330	210,397
1935	17,936	194,706
1936	19,439	187,321

Source: Company records.
May 12, 1937.

Cash	$ 160,651	$ 91,934	$ 82,014	$ 504	$ 175	$ 2,803	$	$	$ 338
Accounts Receivable:									
Railroads	51,748	6,643							58
All Others	147,974	10,308	35,368	2,096	32,195	4,045	250		232
Affiliated Companies	51,867						976	52,842	
Bills Receivable	6,405	2,162	33	790					9
Inventories - Coal, Coke, Supplies, Merchandise, etc.	113,179	22,677	46,391	3,733	18,487	11,884			216
Securities Owned:									
Guaranty Fund - U. S. Bonds Deposited in accordance with Colorado Workmen's Compensation Act	34,788	53,454							88
Stocks of Subsidiary Companies (Par Value)	873,500		8,360					881,860	
Deferred Debit Items	6,828	3,656	172		216				10
Cash Surrender Value of Insurance on Life of A. B. Apperson		5,398							5
Property	14,047,704	1,009,432	60,245	130	15,240	1,192	38,000		15,17
TOTAL	$15,494,644	$1,205,665	$232,582	$ 7,254	$66,313	$19,924	$39,226	$934,702	$16,13
LIABILITIES									
Accounts Payable:									
Pay Rolls, Vouchers, etc.	$ 138,010	$ 21,857	$ 21,028	$ 970	$ 2,822	$ 42	$	$	$ 18
Provision for Federal Income Taxes	885	206	2,174				244		
Affiliated Companies	976			675	43,099	7,983	110	52,842	
Deferred Credit Items	250								
Accrued Expenses	11,140	7,246	758		847	93			2
Reserves	2,735,911	451,135	33,651	128	4,090	770			3,22
CAPITAL STOCK	10,000,000	665,500	150,000	8,360	10,000	10,000	38,000	881,860	10,00
Excess of Par Value over Cost of Stock of Subsidiary Companies	43,599								4
Unrealized Profit				209					
SURPLUS	2,563,872	59,721	24,971	D 3,087	5,454	1,037	872		2,65
TOTAL	$15,494,644	$1,205,665	$232,582	$ 7,254	$66,313	$19,924	$39,226	$934,702	$16,13

Note: D - Decrease or Deficit.

Source: Company Records.

June 4, 1937.

Ton miles revenue freight, normal year	2,659,292
Reduced to amount comparable with 1935 by dividing by 102.524%	2,593,824
Ton miles of cars and company freight required at 1.76139	4,568,736
Ton miles revenue freight, normal year	2,659,292
Gross ton miles, normal year	7,228,028

March 19, 1937

[fol. 1530] EXHIBIT No. 118

Witness: Pyeatt.

The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937

Finance Docket No. 11002

Forecast of Net Income Available for Interest for a Normal Year for The Denver and Rio Grande Western Railroad Company

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Grand Total—Carload Traffic	162
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[fol. 1532]

The Denver and Rio Grande Western Railroad Company

Including the Denver & Salt Lake Western Railroad Company, Goshen Valley Railway Company and the Rio Grande Junction Railway Company

Estimated Amount Available for Interest for a "Normal Year"

	Normal Year	Per cent of Operating Revenues
Railway Operating Revenues:		
Freight	$27,884,000	90.73
Passenger	1,525,000	4.96
Mail	475,000	1.54
Express	300,000	.98
Dining and Buffet	150,000	.49
Other	400,000	1.30
Total Railway Operating Revenues	$30,734,000	100.00
Railway Operating Expenses:		
Maintenance of Way and Structures	$3,955,420	13.00
Maintenance of Equipment	6,146,800	20.00
Traffic	768,350	2.50
Transportation	10,065,385	32.75
Miscellaneous	230,505	.75
General	1,105,424	3.60
Transportation for Investment—Cr.	92,202	.30
Total Railway Operating Expenses	$22,220,682	72.30
Net Revenue from Railway Operations	$8,513,318	
Railway Tax Accruals	2,700,000	
Railway Operating Income	$5,813,318	
Equipment Rents—Net Debit	$600,000	
Joint Facility Rents—Net Debit	265,000	
Total Rents	$865,600	
Net Railway Operating Income	$4,948,318	
Non-Operating Income	300,000	
Gross Income	$5,248,318	
Miscellaneous Deductions	50,000	
Amount Available for Interest	$5,198,318	

[fol. 1533]

EXHIBIT 119

January 18, 1937—Witness Pyeatt

The Denver and Rio Grande Western System

Proposed Plan of Consolidation and Reorganization as of January 1, 1937

Finance Docket No. 11002

[fol. 1585]

EXHIBIT 120

Witness: Pyeatt

The Denver and Rio Grande Western System

Estimated Amount Available for Interest for a "Normal Year"

	Denver and Rio Grande Western R.R. Co.	Per cent of Operating Revenues	Denver and Salt Lake Railway Company	Per cent of Operating Revenues	Denver and Rio Grande Western System	Per cent of Operating Revenues
Operating Revenues:						
Freight	$27,884,000	90.73	$2,790,189	93.4	$30,674,189	90.96
Passenger	1,525,000	4.96	90,000	3.0	1,615,000	4.79
Mail	475,000	1.54	65,000	2.2	540,000	1.60
Express	300,000	.98	12,000	.4	312,000	.93
Miscellaneous	550,000	1.79	30,000	1.0	580,000	1.72
Total	$30,734,000	100.00	$2,987,189	100.00	$33,721,189	100.00
Operating Expenses:						
M. of W. & S.	$3,995,420	13.00	$350,000	11.7	$4,345,420	12.85
M. of Equipment	6,146,800	20.00	568,000	19.0	6,714,800	19.91
Traffic	768,350	2.50	20,000	.7	788,350	2.34
Transportation	10,065,385	32.75	717,600	24.0	10,782,985	31.98
General	1,106,424	3.60	50,000	1.7	1,156,424	3.43
Miscellaneous	230,505	.75			230,505	.68
Transportation for Invest.—Cr.	92,202	.30	8,000	.3	100,202	.30
Total	$22,220,682	72.30	$1,697,600	56.8	$23,918,282	71.49
Net Revenue from Ry. Operations	$8,513,318		$1,289,589		$9,802,907	
Tax Accruals	2,700,000		275,000		2,975,000	
Railway Operating Income	$5,813,318		$1,014,589		$6,827,907	
Equipment Rents Net Debit	600,000		65,000		665,000	
Joint Facility Rents—Net Credit	265,000 Dr.		537,950		272,950	
Total Rents	$865,000 Dr.		$472,950 Cr.		$392,050 Dr.	

EXHIBIT 120—Continued

Witness: Pyeatt
The Denver and Rio Grande Western System
Estimated Amount Available for Interest for a "Normal Year"

	Denver and Rio Grande Western R.R. Co.	Per cent of Operating Revenues	Denver and Salt Lake Railway Company	Per cent of Operating Revenues	Denver and Rio Grande Western System	Per cent of Operating Revenues
Net Railway Operating Income	$4,948,318		$1,487,539		$6,435,857	
Non-Operating Inc.	300,000		20,000		244,040	
Gross Income	$5,248,318		$1,507,539		$6,679,897	
Misc. Deductions from Gross Inc.	50,000		414,474		464,474	
Amount Available for Interest	$5,198,318		$1,093,065		$6,215,423	

NOTE: Inter-Company item eliminated from Non-Operating Income—Interest on $1,266,000 D. & S. L. First Mortgage 6% Bonds—$75,960.

February 6, 1937.

(Here Follows 1 Photolithograph, Side Folio 1537)

THE DENVER AND RIO GRANDE WESTERN SYSTEM
Proposed Plan of Consolidation and Reorganization as of January 1, 1937
Finance Docket No. 11002

UTAH FUEL COMPANY AND SUBSIDIARY COMPANIES
Consolidated Balance Sheet as of December 31, 1936 and 1935

ASSETS	Utah Fuel Company	The Calumet Fuel Company	Wasatch Store Company	Utah Fuel Stoker Sales Company	Bamberger Coal Company	Utah Fuel-Coal Company	Utah Grazing Lands Company	Eliminations	CONSOLIDATION 1936	CONSOLIDATION 1935
Cash	$ 160,651	$ 91,934	$ 82,014	$ 504	$ 175	$ 2,803	$	$	$ 338,082	$ 252,3
Accounts Receivable:										
Railroads	51,748	6,643							58,391	61,3
All Others	147,974	10,308	35,368	2,096	32,195	4,045	250		232,236	250,1
Affiliated Companies	51,867						976	52,842		
Bills Receivable	6,405	2,162	33	790					9,390	12,5
Inventories - Coal, Coke, Supplies, Merchandise, etc.	113,179	22,677	46,391	3,733	18,487	11,884			216,350	214,9
Securities Owned:										
Guaranty Fund - U. S. Bonds Deposited in accordance with Colorado Workmen's Compensation Act	34,788	53,454							88,243	88,2
Stocks of Subsidiary Companies (Par Value)	873,500		8,360					881,860		
Deferred Debit Items	6,828	3,656	172		216				10,872	5,0
Cash Surrender Value of Insurance on Life of A. B. Apperson		5,398							5,398	9,4
Property	14,047,704	1,009,432	60,245	130	15,240	1,192	38,000		15,171,943	15,118,5
TOTAL	$15,494,644	$1,205,665	$232,582	$ 7,254	$66,313	$19,924	$39,226	$934,702	$16,130,904	$16,012,6
LIABILITIES										
Accounts Payable:										
Pay Rolls, Vouchers, etc.	$ 138,010	$ 21,857	$ 21,028	$ 970	$ 2,822	$ 42	$	$	$ 184,729	$ 146,4
Provision for Federal Income Taxes	885	206	2,174				244		3,509	2,5
Affiliated Companies	976			675	43,099	7,983	110	52,842		
Deferred Credit Items	250								250	2
Accrued Expenses	11,140	7,246	758		847	93			20,084	24,6
Reserves	2,735,911	451,135	33,651	128	4,090	770			3,225,685	3,149,8
CAPITAL STOCK	10,000,000	665,500	150,000	8,360	10,000	10,000	38,000	881,860	10,000,000	10,000,0
Excess of Par Value over Cost of Stock of Subsidiary Companies	43,599								43,599	43,5
Unrealized Profit				209					209	1,1
SURPLUS	2,563,872	59,721	24,971	D 3,087	5,454	1,037	872		2,652,838	2,644,1
TOTAL	$15,494,644	$1,205,665	$232,582	$ 7,254	$66,313	$19,924	$39,226	$934,702	$16,130,904	$16,012,6

	CONSOLIDATION		
iminations	1936	1935	Increase
$	$ 338,082	$ 252,391	$ 85,692
	58,391	61,305	2,914 D
	232,236	250,180	17,945 D
52,842			
	9,390	12,547	3,157 D
	216,350	214,950	1,401
	88,243	88,243	
881,860			
	10,872	5,062	5,810
	5,398	9,448	4,050 D
	15,171,943	15,118,543	53,399
$934,702	$16,130,904	$16,012,668	$118,236
$	$ 184,729	$ 146,464	$ 38,265
	3,509	2,552	957
52,842			
	250	250	
	20,084	24,615	4,531 D
	3,225,685	3,149,875	75,810
881,860	10,000,000	10,000,000	
	43,599	43,599	
	209	1,166	957 D
	2,652,831	2,644,147	8,692
$934,702	$16,130,904	$16,012,668	$118,236

[fol. 1538]

R. & I. TRUSTEE'S EXHIBIT 246
Witness: Warner

The Denver and Rio Grande Western Railroad Company Reorganization
Finance Docket No. 11002

Property Values as Derived from Bureau of Valuation Elements of Value as of December 31, 1935, and Rates of Earnings thereon during Test Period computed on basis of Railway Earnings as adjusted on Debtor's Exhibit 113 (Straight Mileage Prorate)

(D denotes Deficit or Debit)

	Net Railway Operating Income 1.	San Luis Valley Potato Adjustment 2.	Miscellaneous Rent Income less Rent for Leased Road 3.	Total of Columns 1, 2, 3 4.	Adjustment for hauling Company Material 5.	Adjusted Income from Railway Operations Amount 6.	% Return on Basis Column 13 Line e. 7.	Line g. 8.
Denver & Rio Grande Western R. R. including Denver & Salt Lake Western R. R., Rio Grande Jct. Ry. and Goshen Valley R. R.)								
Total	2,442,342	182,342	88,398	2,713,081		2,713,081	2.11	
Deduct Narrow Gauge	703,624D		14,370	689,254D	135,443	553,811D		
Standard Gauge Only	3,145,966	182,342	74,028	3,402,335	135,443D	3,266,892		2.94

	Property Values as of December 31, 1935				
	Reproduction Less Depreciation		Lands		Total Cols. 9 to 12 incl.
	Road 9.	Equipment 10.	Carrier 11.	Non-Carrier 12.	13.
a. Denver & Rio Grande Western R. R.	$94,535,747	$20,932,009	$4,333,196	$1,094,963	$120,895,915
b. Denver & Salt Lake Western R. R.	3,880,723		7,219		3,887,942
c. Rio Grande Jct. Ry.	3,409,074		54,006	6,324	3,469,404

R. & I. Trustee's Exhibit 246—Continued

d. Goshen Valley R. R.	270,756		1,908		272,664
e. Total of above	102,096,300	20,932,069	4,396,329	1,401,287	128,525,925
f. Deduct Narrow Gauge	14,958,871	1,974,829	545,078		17,478,778
g. Standard Gauge Only	87,137,429	18,957,180	4,952,538		111,047,147
h. Working Capital not included above					2,473,400
i. Total including Working Capital					113,520,547

The foregoing figures do not include so-called Other Elements of Value. In the Commission's valuation of the D. & R. G. W. properties as of June 30, 1919, Valuation Docket 960, it found a final value of $104,457,348 for total owned property including the Junction and Kenilworth and Heiger R. R. S. or $5,895,803 in excess of the $98,561,545 reproduction less depreciation value plus lands. If, for working capital, and going concern value, etc., there be added to the present standard gauge reproduction less depreciation value plus standard gauge lands of $111,047,147
the entire above figure of 5,895,803
there is obtained as the total figure for the standard gauge 116,942,950

Detail of Narrow Gauge Valuation Deducted in above Schedule to Determine Standard Gauge Valuation

Elements of Value December 31, 1935

	Reprod. Less Deprec.		Lands	
	Road	Equipment	Carrier and Non-Carrier	Total
	14.	15.	16.	17.
Eastern Consols	$14,129,624	$458,898	$532,396	$15,120,918
R. & I.	829,247	1,129,493	12,682	1,971,422
Equipment Trusts		385,973		385,973
Not specifically allocated		465		465
Total Narrow Gauge	14,958,871	1,974,829	545,078	17,478,778

[fol. 1539] Exhibit 253—Witness Burdick

A Valuation of the Utah Fuel Company Properties and of Its Subsidiary Concerns. E. H. Burdick, Mining Engineer & Geologist, Judge Building, Salt Lake City, Utah, 1937.

[fol. 1540] INDEX

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[fol. 1541] History of the Utah Fuel Company

The Utah Fuel Company was organized October 20, 1900 under the laws of the State of New Jersey, with a Capital of $10,000.00 represented by 100 shares of common stock. Capitalization increased October 31, 1900 to $10,000,000.00.

Prior to December 31, 1931 this company acquired the following companies and properties, and continued to operate them as subsidiaries:

1. The Pleasant Valley Coal Company:

Organized under the laws of Utah, September 6, 1882, with a capitalization of $200,000.00, and on August 28, 1890 increased to $2,000,000.00 represented by 20,000 shares of $100.00 each. Acquired October 31, 1900.

At the time of acquisition, the Pleasant Valley Coal Company operated the Winter Quarters, Castle Gate and Clear Creek mines, all in Carbon County, Utah, and had a well established business. It also owned the "Utah Mine" which was the original nucleus of the company. Utah Mine was not working at the time of purchase, but was inter-

mittently operated thereafter until final closure and abandonment in 1925.

2. Wasatch Store Company:

Organized under the laws of the State of Utah, April 8, 1892 with a Capital stock of $25,000.00, divided into 250 shares of $100 each. Later capitalization was increased and at December 31, 1936 there was $150,000.00 stock outstanding.

The Company conducted a general mercantile business and maintained stores at each of the mine units.

3. Holladay Coal Company:

This company was organized March 30, 1897 under the laws of the State of Utah with a capitalization of $200,000.00, represented by 2000 shares of $100.00 each.

Acquired October 31, 1900.

This company was the owner of 2,412.76 acres of coal lands at Sunnyside, Utah and had a mine operating therein when the company was acquired by the Utah Fuel Company.

[fol. 1542] 4. The Calumet Fuel Company:

Organized October 27, 1904 under the laws of the State of Colorado, with authorized capital stock of $1,000,000.00, represented by 1000 shares of $100.00 each.

This company was acquired January 31, 1905 for $624,400.71. At the time of purchase, $665,500.00 of the capital stock had been issued. It was maintained as a separate company and acquired property in six different districts in Colorado and New Mexico.

In addition to the mining unit purchased, there was included a narrow gauge railroad about four miles in length, extending from the mine to a point about three miles from Durango, Colorado, where it connected with the Rio Grande Southern Railroad.

The mine in operation at Perins Peak had been opened up by the Boston Coal and Fuel Company which was acquired by the Calumet Fuel Company January 31, 1905.

5. Sterling Coal and Coke Company:

Organized May 21, 1894 under the laws of Utah, with a capital stock of $300,000.00, represented by 3000 shares of $100.00 each.

Acquired by the Utah Fuel Company February 18, 1908. The lands held by this company consisted of 472.03 acres in the Morrison District, Sanpete County, Utah. After acquisition by the Utah Fuel Company, the Sterling Coal and Coke Company was dissolved, and the property has been carried directly under the Utah Fuel Company.

6. Castle Gate Coal, Coke and Fuel Company:

Organized September 6, 1913 under the laws of the State of Utah, with a capital stock of $100.00, represented by 100 shares of $1.00 each.

This was a corporation formed for the purpose of protecting the trade name "Castle Gate." It has no assets.

Mines Operated as of December 31, 1921

Utah Fuel Company

Sunnyside Mine—(Utah)—The Sunnyside Mine is located [fol. 1543] at the terminus of the Sunnyside Branch of the Denver & Rio Grande Western Railroad, Carbon County, Utah. Throughout the Sunnyside area there are two seams of coal, one above the other separated by a variable rock thickness between them of from six to forty feet. This situation might be more correctly viewed as one seam with a rock "split" of varying thickness within the coal bed itself. Going south, the two parts join and form one seam. The same is true over small areas in the southern part of the Sunnyside mine unit.

The original mine opening was made in May, 1900 on the lower bed by means of a tunnel operation extending inward from the outcrop and within the bed itself, which gently sloped away from the surface exposure. This mine was designated as Mine No. 1. Later a mine was opened on the upper bed and was designated No. 4 Mine. Mines Nos. 1 and 4 discharge onto the same tipple and in addition have underground connections. Like mining attempts were made in the south Sunnyside areas by means of Mines Nos. 2 and 3. These south mines have haulage to the tipple which is separate from that for Mines Nos. 1 and 4. All four mines of the Sunnyside group could properly be considered as one mine.

The Sunnyside mining unit acreage and that extending southward therefrom for about three miles cover practically

all of the known area in Utah containing coal of metallurgical coking quality. Due to this fact, the Sunnyside operations occupied a dominant position in importance among Utah Fuel Company mines.

Area of Sunnyside Unit, 23,475 acres.

Average normal annual output, 670,000 tons.

Quality of coal, bituminous and of coking quality. Its composition is fairly represented by the following proximate analysis:

Proximate Analysis

Moisture	3.9%
Volatile	38.0
Fixed Carbon	53.0
Ash	5.1
	100.0%
Sulphur	.50
B. T. U.	13,520
B. T. U.-Moisture Free	14,070

[fol. 1543a] As of 1921, practically seventy per cent of the mine output was coked upon the ground. The coke equipment consisted of 819 Beehive ovens of six tons coal capacity each and capable of producing 3.3 tons of coke each forty-eight hours.

Somerset Mine—(Colorado)—The Somerset Mine unit is located in Gunnison and Delta counties on the Somerset Branch of the Denver & Rio Grande Western Railroad extending from Delta, Colorado up the north fork of the Gunnison River, a distance of some forty miles. In the vicinity of Somerset, four coal beds are present, the mine being opened on the second above the heavy Rollins Sandstone base. On this latter, the lowest of "A" seam rests, a bed about four feet in thickness. Fifteen feet above is the "Somerset" or "B" seam within the upper 11 to 13 feet of which the mine workings were driven. Thirty to sixty feet higher occurs the 7 to 8 foot "C" seam, 200 feet above which is the 15 to 20 foot "D" seam.

The mine was opened by means of a slope within the gently northward dipping Somerset bed, extending downward along the pitch. By 1921 the main slope had reached a point near the north boundary line of the property, about one and one-quarter miles in from the portal. Thirteen

pairs of entries had been driven east and west from the slope, some of which attained a length of over a mile.

The "cover" or superimposed strata over the deeper workings attained great thickness, being at some points up to 3,000 feet.

In 1920 fires commenced to develop in the mine. These were in all probability due to the extreme pressure of the overburden. These fires could only be controlled by hermetically sealing the general mine area in which they were located. By the end of 1921 possibly one-tenth of the territory opened by the Somerset Mine within the Somerset seam had been sealed off.

Area of the Somerset unit, 3411.93 acres.

Average normal annual output, 275,000 tons.

Tipple capacity 1200 tons, one shift.

Quality of coal, a good grade of bituminous and non-coking in character. Its composition is fairly represented by the following proximate analysis:

[fol. 1544] Proximate Analysis

Moisture	3.5%
Volatile	39.0
Fixed Carbon	52.0
Ash	5.5
	100.0%
Sulphur	.55%
B. T. U.	13,250
B. T. U.—Moisture Free	13,730

Pleasant Valley Coal Company

Castle Gate No. 1 Mine. This mine was opened in 1886 and is situated at Castle Gate on the Denver & Rio Grande Western Railroad. At the time of opening of this mine it was not known that there were any beds of coal other than the bottom or Castle Gate seam which is now known as the "A" bed. The mine was opened by means of a slope following up the pitch of the coal and within the coal bed itself. For many years this mine furnished the major portion of the coal output of the company. Later, workings

were extended to some of the overlying seams which were workable over rather restricted areas. Extraction was accomplished largely by means of room and pillar work.

The coal is a fine grade of bituminous and non-coking in character. It was very satisfactory for both steam and domestic purposes.

The average annual output of this mine was around 170,000 tons. It discharged onto the same tipple over which the product from No. 2 Mine was passed, the Castle Gate No. 1 product coming in at the west end of the tipple and the No. 2 tonnage from the opposite side. The tipple was so constructed that it could handle 1500 tons of coal from No. 1 Mine per eight-hour shift.

A representative analysis follows:

Proximate Analysis

Moisture	2.3%
Volatile	39.4
Fixed Carbon	53.9
Ash	4.4
	100.0%
Sulphur	.76%
B. T. U.	13,441
B. T. U.—Moisture Free	13,757

[fol. 1545] *Castle Gate No. 2 Mine.* This mine is situated at Castle Gate, Utah and was opened in 1911 by means of a tunnel within the coal bed extending easterly about one and one-half miles. The mine was originally opened on the lowest or "A" seam. As this seam thinned going to the east, operations were transferred to the next seam above, designated as the "B" seam, and large quantities of coal mined therefrom on the "raise" side of the main tunnel. Subsequently the presence of the fourth of "D" seam was discovered and as this was a much thicker bed of good quality, operations were transferred to this horizon.

A slope in this coal bed was driven to the north for approximately one mile and nine pairs of entries turned therefrom. The "D" seam, or upper bed, ranged from 10

to 25 feet in thickness. Production from this mine would be limited only by tipple capacity and market.

Tipple capacity as of 1921 from No. 2 Mine was approximately 1500 tons, working one shift, making the joint capacity of Nos. 1 and 2 mines 3000 tons.

Normal average annual production for No. 2 Mine is 236,000 tons. The coal is a good grade of bituminous but inclined to be banded with lenses of bony material.

The following is a representative analysis:

Proximate Analysis

Moisture	2.6%
Volatile	42.7
Fixed Carbon	49.1
Ash	5.6
	100.0%
Sulphur	.36%
B. T. U.	13,180
B. T. U.—Moisture Free	13,533

Clear Creek Mine. This mine is situated at the terminus of the Scofield Branch of the Denver & Rio Grande Western Railroad in what is known as Pleasant Valley. It was opened in July, 1899 by means of entries driven from the outcrop and within the coal bed. There are two workable beds of coal present over this area, the lower known as the Clear Creek Seam which varies from 6 to 14 feet in thickness, and within which the main mine opening was driven. From the mine workings in the lower seam, re- [fol. 1546] stricted development was carried on in the upper bed, but production costs, due to thinness of the bed, precluded profitable operations.

The Clear Creek Mine in its early history was one of the important Utah mines. There was a demand for the product for domestic purposes. The coal is a fair grade of bituminous, but carries a relatively high percentage of water of crystal-ization and hence does not store well.

The average normal annual output of this mine was around 250,000 tons. (Year 1920—271,000; 1921—192,000 tons.)

The following proximate analysis indicates the chemical properties of the coal:

Proximate Analysis

Moisture 221° F.	5.96%
Comb. Vol.	38.2
Fixed Carbon	49.61
Ash	6.16
	100.0%
Sulphur	.393%
B. T. U.	12,591

Utah Mine. This mine is located on the Scofield Branch of the Denver & Rio Grande Western Railroad about four miles north of the Clear Creek and between it and the Winter Quarters Mine. The mine was opened by a tunnel within the Utah coal bed which is probably the same as the lower bed at Clear Creek. The mine was opened in 1882, but was closed in 1884 and up until 1921 had operated only intermittently.

The Utah Mine territory is badly cut up by faults and the coal bed crushed and dislocated. The coal was about the same quality as Clear Creek. For the ten years preceding 1922 the mine averaged 40,867 tons output per year.

Winter Quarters Mine. The Winter Quarters Mine is located in Pleasant Valley on a short switch track from the town of Scofield on the "Scofield Branch" of the Denver & Rio Grande Western Railroad. The mine was opened in 1884 by tunnel and slope workings from the outcrop of the Winter Quarters coal bed and within the same. From the date of opening and until 1921, the mine was worked continuously and many miles of entries and tunnels were driven.

[fol. 1547] The quality of the coal was about the same as that at Clear Creek and Utah mines. It was a fair grade of bituminous with a relatively high percentage of water of crystal-ization. It was inclined to break in handling and was not a good keeper.

A normal average annual output through the life of the mine up to and including 1921 was around 270,000 tons per year.

The tipple had a capacity of 2000 tons per one shift.

A characteristic analysis follows:

Proximate Analysis

Moisture	6.90%
Volatile	43.10
Fixed Carbon	44.80
Ash	5.20
	100.00%
Sulphur	.72%
B. T. U.	12,470
B. T. U.—Moisture Free	13,400

The

The Calumet Fuel Company

Perins Peak Mine. This mine is located about three miles west of Durango, La Plata County, Colorado, near the top of a prominent castle-like mountain known as Perins Peak. There is but one coal bed of sufficient size to work at present within this unit, this ranging in thickness from 4 to 7 feet.

The mine was opened prior to 1906 at the outcrop, and developed by a tunnel in the coal bed 4500 feet long which was driven up the slope. The area tributary is small, as the coal measure truncates Perins Peak and comes to an outcrop entirely around it.

The mine had an average annual production for the ten years prior to 1922 of 52,000 tons. The tipple capacity was 500 tons, operating one shift.

The product was a fine grade of bituminous coal, but inordinately high in sulphur. The output was used on the narrow gauge division of the Rio Grande as well as for domestic purposes.

A typical analysis follows:

[fol. 1548] Proximate Analysis

Moisture	3.64%
Volatile	37.79
Fixed Carbon	53.35
Ash	5.22
	100.00%
Sulphur	1.36%
B. T. U.	13,595

Huerfano County, Colorado, Lands

Pinon and Gross Tract. The Pinon and Gross Tract owned by the Calumet Fuel Company consisted of 4240 acres situated on the Loma Branch of the Denver & Rio Grande Western Railroad extending north from Walsenburg, Colorado. No company operations were maintained in this tract. There were, however, three lease operations: Turner Mine, Gordon Mine and Vesta Mine.

There were no mining operations within the other tracts owned by the Calumet Fuel Company in Colorado and New Mexico.

Changes During Period December 31, 1921 thru December 31, 1936

Utah Fuel Company

Sunnyside Mine. During 1927 the Columbia Steel Company finished the installation of by-product coke ovens at the Columbia Steel plant at Ironton, Utah. In the meantime they had acquired the acreage of coking coal lying to the south of Sunnyside, and had developed a large mine therein. In January 1928 the Columbia Steel Company, through competitive bidding, took over the major coking contracts that formerly had been held by the Utah Fuel Company and supplied from the mines and coke ovens at Sunnyside. This directly deprived the Sunnyside Mine of market for around 200,000 tons of coal per year, the coal to coke ovens dropping to only 9,378 tons in 1936 and the total production of the mine from 478,802 tons in 1922 to 44,589 tons in 1936.

In 1929 the natural gas line was completed into Salt Lake City and surrounding territory. Previously gas had been manufactured from Sunnyside coal. This further reduced the demand on this mine. As a result, the No. 2 Mine area at Sunnyside was abandoned and rails and machinery removed. A large number of the coke ovens were torn down and the others not maintained. Most of the town was dismantled and houses were removed.

[fol. 1549] *Somerset Mine, Colorado.* Spontaneous fires continued to occur in the lower or Somerset seam until the entire east side and the lower part of the west side of the mine was under seal. Mining operations were transferred to the coal bed next above the Somerset measure and pro-

duction as of December 31, 1936 was coming entirely from this upper bed. Production has been well maintained at this mine, the output for 1936 being 210,970 tons as against 261,086 tons as of 1922. The low point of production was reached in 1933 when it dropped to 115,822 tons.

Castle Gate No. 1 Mine. In November, 1929, Castle Gate No. 1 Mine caught fire from an electric short circuit. This fire eventually resulted in the sealing of the entire mine and complete abandonment of operations therein. On account of the topography the pillar areas have caved to surface and it is improbable that this mine can ever be safely reopened and production therefrom established. The loss of this coal area was doubly important because the new Castle Gate tipple which had been completed but a short time before was so designed as to serve both the No. 1 and the No. 2 mines discharging onto the tipple at opposite ends. The failure of No. 1 Mine, unless the design of the tipple is now radically changed, reduces the tipple capacity by about fifty per cent.

Castle Gate No. 2 Mine. On March 8, 1924 a terrific explosion occurred in the Castle Gate No. 2 Mine, killing 172 men and causing a property loss of approximately $280,000.00, and a Workmen's Compensation expenditure of $600,000.00. Another explosion occurred in August, 1928 but as no men were in the mine there was no loss of life. The physical damage amounted to approximately $127,000.00. As a result of the original explosion, the workings down the pitch of the coal seam were sealed off and have so remained to the present time. The main-line mine tunnel was extended to the east and production is now coming from that territory.

Utah Mine. The Utah Mine was finally closed down and abandoned and the Utah Mine settlement dismantled February, 1925.

Winter Quarters Mine. In July, 1928 the entire Winter Quarters Mine and camp was abandoned. Material and machinery were taken from the mine and all surface equipment and buildings were removed.

On September 6, 1932 the charter of the Pleasant Valley Coal Company expired and all assets were deeded to the Utah Fuel Company.

[fol. 1550] In 1923 a new small shaft mine was opened at Castle Gate. This is producing coal from a coal bed above that worked in the Castle Gate No. 2 Mine. This

mine has not been operated steadily but has been used for supplementary supplies when market demanded.

As of December 31, 1936 the Utah Fuel Company had only the following operating mines:

(1) Somerset Mine, Colorado
(2) Sunnyside Mines, operating at 40% former capacity
(3) Castle Gate No. 2 Mine
(4) Clear Creek Mine, at 50 to 60 per cent capacity.

The shrinkage of total coal demand caused such an extent that the unit tax load reached prohibitive proportions, being in excess of twenty three cents per ton. Practically all of the coal land held had been acquired when the system of taxation in Utah imposed but a very slight burden on carrying charges. Under the circumstances then prevailing it was deemed wise to acquire a very large acreage even though the coal contained could not be marketed for a hundred years or more.

Developments in the Rocky Mountain coal fields, particularly in Utah and in western Colorado, have demonstrated that it is very questionable whether coal under overburden in excess of 1500 to 1800 feet can be mined at a profit over large areas. It was, therefore, deemed advisable to let those lands in which the coal was deeply buried or would be reached for many years to come, go for taxes, the company retaining the control of the surface.

In addition to the reasons above stated, the areas back from the outcrop which were within abandoned mine territory, were allowed to be tax delinquent and will revert to the county in which they are situated by June 1 of this year.

13,681.66 acres within or adjacent to the original mine units in Carbon County were allowed to become tax delinquent. The taxes on the 472.03 acres in the Morrison District, Sanpete County, were also allowed to become delinquent.

On December 5, 1932 the Utah Grazing Lands Company was incorporated under the laws of the State of Utah with authorized capital of $50,000.00, represented by 10,000 shares of common stock of $5.00 each. December 31, 1936 there was $38,000.00 capital stock outstanding.

The sole purpose of this company was to administer the [fol. 1551] surface of those lands within which the coal

right had been relinquished. As of December 31, 1936 these surface rights totaled 37,214.66 acres.

The Calumet Fuel Company

Perins Peak Mine. On December 8, 1926 the Perins Peak Mine, La Plata County, Colorado, became exhausted and was abandoned.

Huerfano County, Pinon and Gross Tract

Calumet No. 1 Mine. The Turner Mine which had been operating under lease in the Pinon and Gross Tract was acquired by the Calumet Fuel Company on September 1, 1922. This mine operated practically continuously until December 18, 1933, when it was closed down.

In the early twenties a lease had been granted on a tract of ground within the Pinon and Gross Tract adjoining the Turner Mine. This was known as the Brennan Mine. On April 26, 1924 the Brennan Mine was taken over by the Calumet Fuel Company and became the Calumet No. 2 Mine.

Of the 1367 acres owned in the Florida District, La Plata County, Colorado, 913.83 acres were sold. In the remaining acreage the coal rights were relinquished but surface retained, as was also the 601 acres composing the worked-out Perins tract. The 160 acres owned in San Juan County, New Mexico, were allowed to go for taxes.

As of December 31, 1936 the Calumet Fuel Company was operating one mine, the Calumet No. 2.

[fol. 1552] Utah Fuel Company Valuation

Depreciable Property

Herewith on page 52 is a tabulation of all of the depreciable property of the Utah Fuel Company attached and related to their mining operations. A careful comparison of depreciated values with a reasonable going concern value of the various units, showed that broadly speaking, the former portrayed, in my judgment, a reasonable going concern value for most of the items. The most important exception was that of housing. Through the State Tax Commission, the State of Utah has built up a careful and quite accurate system of valuing houses. This value more nearly represents the true present day worth of these structures than the depreciated totals on the books of the com-

pany. Each main item was considered separately, and where thought necessary, corrections were made. At the Somerset Mine of the Utah Fuel Company located in Gunnison County, Colorado, no such near exact system is in vogue. Adjustment of book values for the Somerset Camp were made to conform to those set up in Utah.

Value of Coal Lands

The value of coal lands in this case rests upon three factors: (1) Expectancy of output. (2) Rate of production and life of mine. (3) Reasonable profit per ton.

Regarding (1)

A study has been made of the past history of production of the State of Utah and the relation between Utah Fuel Company production and that of the entire Utah field. This original relation was greatly modified by the loss of the tonnage from the Sunnyside Mine. In my opinion, it is doubtful that any large portion of the coke business will ever be regained. The ratio of Utah Fuel production to the State production, less coking coal output, was deemed the proper basis of comparison. It is worthy of note that under the management of the last few years the Utah Fuel proportion has materially risen to an average of 20% for the last five years.

The output of coal in Utah has been seriously curtailed by three main factors: (1) The wealth of cheap oil from Texas and California; (2) The advent of natural gas in the more populace centers of the State, and (3) the general stagnation of business.

An examination of the history of production and a consideration of the probable modifications of the depressing [fol. 1553] factors leads me to the conclusion that by about 1945 the production of the State will be between 5,000,000 or 6,000,000 tons per year exclusive of that tonnage produced for coke-making purposes. If this assumption is correct, the Utah Fuel Company production in Utah should aggregate 1,200,000 tons per year. To this should be added such an annual output as is justified by the production record and coal reserves at the Somerset Mine in Colorado. This output I would place at 220,000 tons per year, making a total sustained average production through the forty years assumed life of the mine, of 1,420,000 tons. On this basis there would be produced 56,800,000 tons of coal.

Regarding (2)

In years past, many calculations as to mineable reserves in Utah Fuel ground have been made. These have all had to be revised downward as mining work progressed or diamond drill holes were sunk. During the past year, careful estimates were made of the mineable reserves in Colorado and Utah. These reserves have been tabulated in detail by the Engineering Department of the Utah Fuel Company and have been roughly checked by me. Inasmuch as they are greatly in excess of any reasonable requirements which are assumed for the forty-year period, their maximum amount is not of prime importance. The detail of these tabulations will be presented in the complete report but are here set down only in total.

Recoverable coal reserves in Utah, after allowance has been made for coal lands tax delinquent, 81,015,700 tons.

Recoverable tonnage Somerset District, Colorado, 40,400,000 tons.

Regarding (3)

In the early days of the Utah Fuel Company, it exercised a practical monopoly in the Utah field. The net income per ton was large, and contributing to that total in major extent was the Sunnyside Mine and the jointly operated coke ovens. From 1910 to 1920 many new mines were opened in Utah. War demand stimulated large mine developments until today capacity is probably 300% of demand. This has resulted in very sharp competition and the lowering of net realization.

In addition, a new taxing structure was created in 1919 resulting in the unit tax load being increased five to ten fold.

Another condition which has lowered realization in the last few years and will continue to do so is the development of automatic burning equipment using slack coal. This [fol. 1554] development has been in both the industrial and the domestic field. I have studied the yearly sums of net income per ton before charging depletion and depreciation, and it appears to me that the average net income per ton shown by operation from 1928 through 1936 gives a fair key as to what may be expected in the future. The average net income per ton, before depreciation and depletion, of the Utah Fuel Company for this priod was 33.7¢. Depreciation through the forty-year period used as life of the

future operation was taken as 16¢ per ton, which is ample for the tonnage involved. A depletion charge of 3¢ per ton was assumed.

Summary

Value coal per ton after depreciation and depletion	$ .147
Net Value, 56,800,000 tons at $0.147	8,349,600.00
Life of Operation, 40 years.	
Net return per year	208,740.00
Which on basis of 6% return on investment gives a total value of land and plant of	3,479,000.00
Less adjusted book value of plant	1,641,460.00
Value of Coal Lands	$1,837,540.00
Add—Assumed residual value of coal in land after completion of 40-year operation	50,000.00
Total	$1,887,540.00

For Calumet Fuel Company See Page 28.

[fol. 1555] The Calumet Fuel Company Valuation.

Depreciable Property

As in the case of the Utah Fuel Company, the book value of each item of Depreciable Property was considered separately and proper adjustment made.

Value of Coal Lands

It will be recalled that in the case of The Calumet Fuel Company, the Perins Peak property near Durango, Colorado, has been worked out and the mine abandoned. The New Mexico acreage had been allowed to revert to San Juan County, New Mexico for taxes and the coal rights surrendered on the Florida tract, and part of the surface sold. The Forbes tract had also been surrendered for taxes. On the Pinon and Gross Tract the original Turner Mine, afterwards known as Calumet No. 1 Mine, had been closed down and the area logically tributary to this opening, largely exhausted. The only company operation, therefore, as of December 31, 1936 was the Calumet No. 2 Mine adjoining the Calumet No. 1 on the south.

Here again the value of the coal land and the mining plant rests upon (1) expectancy of output, (2) rate of production and life of mine, and (3) reasonable profit per ton, or in lieu thereof a reasonable royalty value.

Concerning 1 and 2

Previously in this report it was stated that the workings of the Calumet No. 2 Mine were principally within the Cameron coal seal or bed. This is relatively thin, ranging from forty-four inches to around five feet. The quality of the coal, however, is excellent and the coal mines with a high percentage of lump and nut. Independent of railroad use, I believe there will be a steady demand for a material tonnage for domestic use both in Colorado and western Kansas and Nebraska.

I have assumed that an average output of 100,000 tons per year can be maintained during the life of the mine.

Developments within the Pinon and Gross tract and away from the outcrop have been disappointing. The acreage held by the Calumet Fuel Company has been explored by diamond drill. The various coal beds do not maintain their thickness away from the outcrop within the area owned. From these explorations, the best present day estimates assign only 2,000,000 tons of recoverable coal remaining. This would give a twenty-year life to the Calumet No. 2 [fol. 1556] operations. For the purpose of valuation this figure is used.

Concerning 3

What the unit profit might be from the Calumet No. 2 Mine is difficult to forecast because the operating history of this property on the Cameron seam is very limited. The Calumet No. 1 Mine was opened on the Walsenburg seam which had a thickness up to seven feet or more. This height, with the general mining conditions, allowed a relatively low production cost which was also made possible by a large and sustained railroad contract. Cost records of the Calumet No. 2 Mine taken by themselves preclude any profitable operation, but it must be borne in mind that the mine had just been reopened and re-equipped.

In view of these circumstances, I consider it more accurate in this case to calculate value of coal lands on a going royalty basis. The prevailing royalty in this district is 10¢

per ton and I have, therefore, fixed coal land value on the basis of present value of 2,000,000 tons recoverable over a twenty-year period at a 10¢ royalty. This value plus the present value of surface plant and equipment is herein considered as the total value of mining unit.

Summary

Recoverable Coal Reserves	2,000,000 tons
Royalty $0.10 per ton	
Annual Mine Production	100,000 tons
Life of Mine	20 years
Present value $0.10 royalty	
20 years at 6%	.057349
Total present value of coal lands	$114,698.00
Adjusted value of plant and equipment	172,385.00
Total Value	$287,083.00

[fol. 1557] Conclusions as to Value

In view of all the foregoing, I place the valuation of the Utah Fuel Company and its subsidiaries at $4,653,720.30 as per the following summary:

Going-Concern Valuation of the Utah Fuel Company (and Subsidiaries)

Capital Stock at December 31, 1936 is summarized as follows:

Lands:		
Utah Fuel Company	$1,899,281 00	
The Calumet Fuel Company	114,698 00	
Utah Grazing Lands Company	88,808 00	$2,102,787 00
Depreciable Property:		
Utah Fuel Company	$1,641,459 99	
The Calumet Fuel Company	172,384 99	
Wasatch Store Company	27 593 77	
Utah Fuel Stoker Sales Company	81 73	
Bamberger Coal Company	11,149 76	
Utah Fuel—Coal Company	422 13	$1,853,092 37
Other Assets—Consolidated:		
Cash	$338,082 49	
Accounts and Bills Receivable	299,016 81	
Inventories—Fuel, Supplies and Merchandise	216,350 48	
Securities Owned—U. S. Bonds	88,242 51	
Deferred Debit Items (Detail Attached)	10,871 68	
Cash Surrender Value of Life Insurance	5,397 75	$957,961 72
Total		$4,913,841 09
Less:		
Accounts Payable	$188,237 99	
Deferred Credit Items (Detail Attached)	329 03	
Accrued Expenses (Detail Attached)	20,084 00	
Reserve for Workmen's Compensation	7,870 48	
Excess of Par Value over Cost of Stock of Subsidiary Companies	43,599 29	$260,120 79
Total Going-Concern of the Utah Fuel Company (and Subsidiaries) Capital Stock at December 31, 1936, More Fully Detailed on Balance Sheets and Statements Herewith		$4,653,720 30

Respectfully submitted,

E. H. Burdick.

EXHIBIT No. 262

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

D. & R. G. W. Earnings Restated on Basis of 1940 Unit Costs

Line No.		1936	1937	1938	1939	1940	1936-1940 Total
1.	Gross Operating Revenue	$25,599,309	$26,781,922	$23,404,171	$25,073,040	$26,219,196	$127,077,708
2.	Thousand Gross Ton Miles in Freight Trains	6,074,599	6,450,663	5,411,271	5,970,436	6,530,335	30,437,304
3.	Freight Operating Expense, 1940					$16,306,894	
4.	Freight Operating Expense per Thousand Gross Ton Miles, 1940					$2.49709915	
5.	Restated Freight Operating Expense, at 1940 Average Cost per Thousand Gross Ton Miles	$15,168,876	$16,107,945	$13,512,480	$14,908,771	$16,306,894	$76,004,966
6.	Passenger Miles	97,230,219	105,171,173	91,158,727	101,113,103	99,887,601	494,560,823
7.	Passenger Operating Expense, 1940					$4,171,977	
8.	Passenger Operating Expense per Passenger Mile, 1940					$.04176672	
9.	Restated Passenger Operating Expense, at 1940 Average Cost per Passenger Mile	$4,060,987	$4,392,655	$3,807,401	$4,223,163	$4,171,977	$20,656,183
10.	Total Restated Operating Expense as above	$19,229,863	$20,500,600	$17,319,881	$19,131,934	$20,478,871	$96,661,149
11.	Net Operating Revenue, Restated	6,369,446	6,281,392	6,084,290	5,941,106	5,740,325	30,416,559
12.	Railway Tax Accruals	$2,247,427	$2,179,587	$2,623,602	$2,227,210	$2,246,045	$11,523,871
13.	Hire of Equipment, Net	582,641	460,067	551,183	597,580	430,843	2,622,314
14.	Joint Facility Rents, Net	260,468	299,958	315,778	318,772	302,279	1,497,255
15.	Other Income, Net (See Footnote)	Cr. 71,373	Cr. 77,047	Cr. 32,227	Cr. 36,843	Cr. 39,356	Cr. 256,846
16.	Total Deductions from Operating Revenue	$3,019,163	$2,862,565	$3,458,336	$3,106,719	$2,939,811	$15,386,954
17.	Available for Interest	$3,350,283	$3,418,827	$2,625,954	$2,834,387	$2,800,514	$15,029,965

NOTE:—Included in "Other Income, Net" are: Interest on $1,266,000, principal amount, D. & S. L. Income Bonds; and dividends on D. & S. L. W. RR. Co. and Denver Colorado Springs Pueblo Motor Way, on same return basis that appears in 1940 accounts. Deductions from "Other Income" include $100,000 for rental of Rio Grande Junction Railway and $146,036 for rental of D. & S. L. W. line. Deduction from net income for "Interest on Unfunded Debt" arbitrarily charged at $20,000 each year to cover only interest on deferred installments of assessments for publi improvements, etc.

Office of Trustees
Denver, Colorado
May 14, 1941

[fol. 1559]

EXHIBIT No. 263

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

D. & S. L. 1936–1940 Earnings Restated on Basis of 1940 Unit Costs

Line No.		1936	1937	1938	1939	1940	1936–1940 Total
1.	Gross Operating Revenue	$2,856,949	$2,806,256	$2,264,604	$2,290,818	$2,363,251	$12,581,878
2.	Thousand Gross Ton Miles in Freight Trains	505,954	542,142	405,806	410,321	452,549	2,316,772
3.	Freight Operating Expense, 1940	.....	.....	.....	.....	$1,549,348	.....
4.	Freight Operating Expense per Thousand Gross Ton Miles, 1940	.....	.....	.....	.....	$3.4236028	.....
5.	Restated Freight Operating Expense, at 1940 Average Cost per Thousand Gross Ton Miles	$1,732,186	$1,856,079	$1,389,319	$1,404,776	$1,549,348	$7,931,708
6.	Passenger Miles	5,036,077	4,424,579	4,341,241	3,411,776	3,522,910	20,736,583
7.	Passenger Operating Expense, 1940	.....	.....	.....	.....	$232,781	.....
8.	Passenger Operating Expense per Passenger Mile, 1940	.....	.....	.....	.....	$.06607634	.....
9.	Restated Passenger Operating Expense, at 1940 Average Cost per Passenger Mile	$332,766	$292,360	$286,853	$225,438	$232,781	$1,370,198
10.	Total Restated Operating Expense as above	$2,064,952	$2,148,439	$1,676,172	$1,630,214	$1,782,129	$9,301,906
11.	Net Operating Revenue, Restated	791,997	657,817	588,432	660,604	581,122	3,279,972
12.	Railway Tax Accruals	$270,548	$317,277	$353,311	$349,804	$203,193	$1,494,133
13.	Hire of Equipment, Net	97,324	109,625	48,048	50,230	21,084	326,311
14.	Joint Facility Rents, Net	Cr. 540,402	Cr. 572,959	Cr. 584,330	Cr. 601,064	Cr. 554,448	Cr.2,853,203
15.	Other Income, Net	Dr. 424,240	Dr. 448,367	Dr. 427,222	Dr. 407,520	Dr. 401,522	Dr.2,108,871
16.	Total Deductions from Operating Revenue	$251,710	$302,310	$244,251	$206,490	$71,351	$1,076,112
17.	Available for Interest	$540,287	$355,507	$344,181	$454,114	$509,771	$2,203,860

Office of Trustees
Denver, Colorado
May 21, 1941

[fol. 1560]

EXHIBIT No. 264

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees.

Combined D. & R. G. W. and D. & S. L. Earnings, 1936–1940, Restated on Basis of 1940 Unit Costs

	1936	1937	1938	1939	1940	1936-1940 Total
Income Available for Interest Restated on Basis of 1940 Unit Costs:						
D. & R. G. W. Railroad	$3,350,283	$3,418,827	$2,625,954	$2,834,387	$2,800,514	$15,029,965
D. & S. L. Railway	540,287	355,507	344,181	454,114	509,771	2,203,860
Total D. & R. G. W. and D. & S. L.	$3,890,570	$3,774,334	$2,970,135	$3,288,501	$3,310,285	$17,233,825

NOTE: No savings have been estimated from consolidation of the two properties.

Office of Trustees
Denver, Colorado
May 14, 1941

[fol. 1561]

EXHIBIT No. 268

The Denver and Rio Grande Western Railroad Company

Wilson McCarthy and Henry Swan, Trustees

Statement of Actual Expenditures for Road and Equipment
(Exclusive of Retirements)

November 1, 1935 to March 31, 1941

Class No.	Description	Nov. 1, 1935 to Dec. 31, 1935	1936	Nov. 1, 1935 to Dec. 31, 1936	1937	1938	1939	1940	Jan. 1, 1941 to Mar. 31, 1941	Jan. 1, 1937 to Mar. 31, 1941	Nov. 1, 1935 to Mar. 31, 1941
1	Widening Cuts and Fills Riprapping, Roadbed Protection, etc.	3,933	133,318	137,251	46,777	52,797	42,942	31,959	1,613	170,088	307,339
2	Ballasting	751	148,451	149,202	490,527	12,024*	176,034	96,561	.....	751,098	900,300
3	Rails and Other Track Material	17,265	309,523	326,788	430,496	160,557	523,105	302,937	2,043	1,419,138	1,745,926
4	Bridges, Trestles and Culverts	20,742	354,717	375,459	161,339	169,925	88,627	122,552	1,911	544,354	919,813
5	Tunnel and Subway Improvements	4,582	.....	4,582	4,818	.....	.....	.....	.....	4,818	9,400
10	Additional Yard Tracks, Sidings, and Industry Tracks	580	213,763	244,343	462,461	39,874	19,860	81,366	2,158	605,719	850,062
11	Changes of Grade or Alignment	.....	64,201	64,201	329,694	22,865	16,135	51,420*	.....	317,274	381,475
12	Signals and Interlocking Plants	.....	42,981	42,981	234,670	6,940	652*	37,407	1,116	279,481	322,462
13	Telegraph and Telephone Lines	.....	24,659	24,059	88,280	1,379	22,078	60,080	1,814	173,631	197,720
14	Roadway Machinery and Tools	.....	38,931	38,931	79,911	51,041	24,118	26,141	22,405	203,616	242,547
15	Section Bldgs & Other Roadway Property	.....	412	412	3,824	363	3,045	5,225	488	12,945	13,357
16	Fences & Snowsheds, Right-of-way, Snow or Sand Fences	.....	420	420	204	461	2,267*	2,892	.....	1,290	1,710
17	Frts and Pssr. Stations, Office, Bldgs. and Other Station-Facilities	10,447	63,249	73,696	108,225	31,074	64,217	50,909	21,109	275,534	349,230
18	Hotels and Restaurants	.....	.....	.....	34,476	.....	200	.....	.....	34,676	34,676
19	Fuel Stations and Appurtenances	.....	172	172	7,340	29	386	4,220	.....	11,975	12,147
20	Water Stations and Appurtenances	.....	24,455	24,455	60,451	6,008	19,968	35,387	4,455	126,269	150,724
21	Shop Buildings, Enginehouses and Appurtenances	.....	28,333	28,333	242,713	41,408	47,001	62,303	8,863	402,291	430,624
22	Shop Machinery and Tools	.....	75,571	75,571	136,621	178,348	63,294	83,085	4,664	480,012	561,583
23	Electric Power Plants, Substations, Trans. & Distr. Lines	.....	.....	.....	.....	.....	1,518	6,480*	7,285	2,323	2,323
27	Real Estate	2,500	2,500	5,000	.....	1	2	.....	.....	3	5,003
28	Public Improvements—Construction	.....	9,673	9,673	26,114	2,921	4,099	11,469	436	45,039	54,712
34	All Other Improvements	.....	.....	.....	294	.....	.....	.....	.....	294	294
35	Locomotives—Steam	.....	.....	.....	568,419	2,023,048	.....	.....	440	2,591,907	2,591,907
36	Locomotives—Other	.....	.....	.....	.....	.....	.....	.....	81,515	81,515	81,515
37	Freight Train Cars	.....	209,981	209,981	684,694	6,214	1,793,819	2,219,637	872,158	5,576,522	5,786,503
38	Passenger Train Cars	.....	204,809	204,809	108,851	373*	119,108	.....	9	227,595	432,404
39	Work Equipment	130	40,299	40,429	81,044	5,001	19,408	35,698	15,305	156,456	196,885
42	Miscellaneous Equipment	.....	264	264	4,208	3,888	3,919	6,725	2,374	21,114	21,378
43	Improvements to Existing Equipment	3,969	176,202	180,171	256,328	30,981	50,008	178,876	30,534	546,727	726,898
44	Const. of Extensions, Branches and Other New Lines	.....	.....	.....	.....	176,274	.....	2,945*	.....	173,329	173,329
	Total Road and Equipment	64,899	2,196,314	2,261,213	4,666,779	2,999,000	3,099,975	3,394,584	1,082,695	15,243,033	17,504,246
	Total Road & Structures (1–34 & 44)	60,800	1,564,759	1,625,559	2,963,235	930,241	1,113,713	953,648	80,360	6,041,197	7,666,756
	Total Equipment (35–43)	4,099	631,555	635,654	1,703,544	2,068,759	1,986,262	2,440,936	1,002,335	9,201,836	9,837,490

* Credit

[fol. 1562]

EXHIBIT No. 269

The Denver and Rio Grande Western Railroad Company

Wilson McCarthy and Henry Swan, Trustees

Statement of Actual Expenditures for Operating Expenses in Connection with Improvements

November 1, 1935 to March 31, 1941

Class No.	Description	Nov. 1, 1935 to Dec. 31, 1935	1936	Nov. 1, 1935 to Dec. 31, 1936	1937	1938	1939	1940	Jan. 1, 1941 to Mar. 31, 1941	Jan. 1, 1937 to Mar. 31, 1941	Nov. 1, 1935 to Mar. 31, 1941
	Widening Cuts and Fills, Riprapping, Roadbed										
1	Protection, etc.	2,141	7,306	9,447	3,770	11,746	2,971	5,346	18	23,851	33,298
2	Ballasting		60,021	60,021	174,731	2,682	68,853	82,085	334	328,685	388,706
3	Rails and Other Track Material	30,010	358,527	388,537	507,097	204,360	738,648	444,674	77,711	1,902,490	2,290,937
4	Bridges, Trestles and Culverts	18,079	225,658	243,737	164,893	110,891	98,822	120,792	1,641	497,039	740,776
10	Additional Nd. Tracks, Sidings and Industry Tracks		16,590	16,590	76,519	19,957	104,277	31,493	85	222,331	238,921
11	Changes of Grade or Alignment		78,276	78,276	200,807	9,291	4,691	127,182		341,924	420,197
12	Signals and Interlocking Plants		7,933	7,933	16,535	13,922	9,031	5,747	448	45,686	53,619
13	Telegraph and Telephone Lines				668	590	753	466		2,477	2,477
14	Roadway Machinery and Tools				10,444	12,671	21,348	7,241	304	52,008	52,008
15	Section Bldgs. & Other Rdwy. Property				262	157	247	1,578		2,244	2,244
16	Fences & Snowsheds—Right-of-way, Snow or Sand Fences						3,961	2*		3,959	3,959
17	Frt. & Pssr. Stations, Office Bldgs. and Other Station Facilities	2,309	19,561	21,870	9,373	29,005	53,646	21,714	12,716	126,544	148,414
18	Hotels and Restaurants				155					155	155
19	Fuel Stations and Appurtenances		100	100	1,928		17*	1,194		3,105	3,205
20	Water Stations and Appurtenances		26,613	26,613	70,521	5,061	11,146	22,247	5,665	114,640	141,253
21	Shop Buildings, Enginehouses and Appurtenances		10,383	10,383	258,713	4,972	6,423	88,081	6,317	264,506	274,889
22	Shop Machinery and Tools		25,414	25,414	15,627	30,904	13,713	32,389	2,506	95,139	120,553
23	Electric Power Plants, Substations, Trans. and Distr. Lines						1,818	7,767		9,585	9,585
28	Public Improvements—Construction				3,770	4,375	113*	2,592*		5,440	5,440
38	Passenger Train Cars					1,755				1,755	1,755
42	Miscellaneous Equipment					66	270			336	336
43	Improvements to Existing Equipment	6	72,211	72,217	135,420	151,712	43,408	50,941	25,380	406,861	479,078
	Total O. E. for Improvements	52,545	908,593	961,138	1,551,143	604,207	1,183,899	1,048,293	63,125	4,450,667	5,411,805
	Total Road & Structures (1-28)	52,539	836,382	888,921	1,415,723	450,674	1,140,221	997,352	37,745	4,041,715	4,930,636
	Total Equipment (38, 42 and 43)	6	72,211	72,217	135,420	153,533	43,678	50,941	25,380	408,952	481,169

* Credit

[fol. 1563] EXHIBIT No. 270

The Denver and Rio Grande Western Railroad Company

Wilson McCarthy and Henry Swan, Trustees

Principal Items of New Equipment Acquired, November 1, 1935-December 31, 1940

Purchased	Built
5 Passenger Locomotives	300 Stock Cars
10 Freight Locomotives	20 Cabooses
900 Box Cars	6 Miscellaneous
100 Auto Box Cars	
100 Ballast Cars	Rebuilt
50 Gondola Cars	58 Passenger Cars
7 Tank Cars	78 Auto Cars
14 Units Work Equipment	

Converted

77 Beet Cars
13 Flat Cars
2 Drovers Cars
133 Work and Outfit Cars

Denver, Colorado, May 17, 1941.

Vol. 1364

EXHIBIT No. 272

Witness: Thompson

The Denver and Rio Grande Western Railroad Company

Comparative Statement of Revenue Traffic Shown in Tons

Years 1920 to 1940, both Inclusive

	Revenue Tonnage Originating on Rio Grande						Revenue Tonnage Received from Connections						
	Terminating on Rio Grande	% of Total	Delivered to Connections	% of Total	Total	% of Total	Terminating on Rio Grande	% of Total	Delivered to Connections	% of Total	Total	% of Total	Total Revenue Traffic Carried
1940	3,158,420	33.74	2,212,889	23.68	5,371,309	57.38	1,630,191	17.41	2,360,510	25.21	3,990,701	42.62	9,362,010
1939	2,957,154	34.38	2,099,759	24.41	5,056,913	58.79	1,522,912	17.71	2,021,174	23.50	3,544,086	41.21	8,600,999
1938	2,678,675	33.74	2,102,447	26.48	4,781,422	60.22	1,379,244	17.37	1,779,417	22.41	3,158,661	39.78	7,940,083
1937	3,358,184	34.32	2,439,940	24.93	5,798,124	59.25	1,720,599	17.58	2,267,891	23.17	3,988,490	40.75	9,786,614
1936	2,975,116	33.39	2,314,611	25.97	5,289,727	59.36	1,517,293	17.03	2,104,913	23.62	3,622,206	40.64	8,911,933
1935	2,512,950	35.00	1,891,624	26.35	4,404,574	61.35	1,288,312	17.95	1,486,139	20.70	2,774,451	38.65	7,179,025
1934	2,448,544	32.48	1,777,505	28.19	3,826,049	60.67	1,108,569	17.58	1,371,740	21.75	2,480,309	39.33	6,306,358
1933	1,831,647	31.45	1,760,419	30.22	3,592,066	61.67	1,032,591	17.73	1,199,686	20.60	2,232,277	38.33	5,824,343
1932	1,667,771	28.96	1,848,232	31.52	3,516,003	60.18	1,205,724	20.56	1,111,364	18.96	2,317,088	39.52	5,863,091
1931	2,169,621	28.89	2,453,481	32.66	4,623,102	61.55	1,639,839	21.83	1,248,011	16.62	2,887,850	38.45	7,510,952
1930	3,029,437	30.80	3,235,436	32.90	6,264,873	63.70	1,974,813	20.08	1,594,638	16.22	3,569,451	36.30	9,834,324
1929	3,655,100	32.07	3,902,239	34.23	7,557,339	66.30	2,194,960	19.26	1,646,103	14.44	3,841,063	33.70	11,398,402
1928	3,546,476	33.14	3,605,803	33.69	7,152,279	66.83	2,080,307	19.44	1,469,472	13.73	3,549,779	33.17	10,702,058
1927	3,977,631	37.36	4,110,657	38.61	8,088,288	75.97	1,687,056	15.84	871,606	8.19	2,558,662	24.03	10,646,950
1926	4,202,062	38.82	4,072,450	37.62	8,274,512	76.44	1,779,426	16.44	770,559	7.12	2,549,985	23.56	10,824,497
1925	4,418,201	40.15	4,121,045	37.45	8,539,246	77.60	1,763,888	16.03	700,550	6.37	2,464,438	22.40	11,003,684
1924	4,340,811	41.38	4,043,255	38.55	8,384,066	79.93	1,523,830	14.53	581,544	5.54	2,105,374	20.07	10,489,440
1923	4,328,811	42.59	4,171,394	41.05	8,500,205	83.64	1,179,075	11.60	483,213	4.76	1,662,288	16.36	10,162,493
1922	3,736,549	38.74	4,464,024	46.29	8,200,573	85.03	1,012,139	10.50	431,385	4.47	1,443,524	14.97	9,644,097
1921	3,527,306	41.45	3,595,307	42.25	7,122,613	83.70	941,613	11.07	445,399	5.23	1,387,012	16.30	8,509,625
1920	4,526,712	37.88	5,313,211	44.45	9,839,923	82.33	1,281,614	10.72	830,716	6.95	2,112,330	17.67	11,952,253

Source: Years 1920–1939 from Exhibit #1 of Witness Thompson introduced at Court Hearing at Denver, Colorado, beginning July 29, 1940; year 1940 Form A Annual Report to Interstate Commerce Commission.

[fol. 1565]

EXHIBIT No. 273
Witness: Thompson

The Denver and Rio Grande Western Railroad Company

Cars and Revenue of Freight Traffic Interchanged with Eastern Connections at Denver and Pueblo Gateways Received from and Delivered to the Southern Pacific at Ogden, Union Pacific at Provo, Salt Lake City and Ogden, and Western Pacific at Salt Lake City, Years 1937–1938–1939 and 1940

	1940		1939		1938		1937	
Eastbound—Via Denver D&RGW Delivered to:	Cars	Thousand Dollars	Cars	Thousand Dollars	Cars	Thousand Dollars	Cars	Thousand Dollars
A. T. & S. F.	287	29	275	24	147	14	162	14
C. B. & Q.	13,476	1,225	10,412	940	8,387	778	10,116	872
C. R. I. & P.	7,616	692	6,731	633	5,603	529	7,042	612
Colo. & Sou.	279	25	221	20	222	19	210	18
Union Pacific	1,492	149	1,290	134	1,334	129	1,307	134
Total	23,150	2,120	18,929	1,751	15,693	1,469	18,837	1,650
Ratio to 1937		128.5%		106.1%		89.0%		100.0%
Westbound—Via Denver D&RGW Received from:								
A. T. & S. F.	77	9	47	5	20	2	33	4
C. B. & Q.	11,214	1,349	9,567	1,242	7,342	950	7,622	952
C. R. I. & P.	3,661	449	3,000	372	2,213	280	2,951	358
Colo. & Sou.	163	15	155	15	89	10	56	7
Union Pacific	941	130	908	136	624	88	758	96
Total	16,056	1,952	13,677	1,767	10,288	1,330	11,420	1,417
Ratio to 1937		137.8%		124.7%		93.5%		100.0%

[fol. 1566]

EXHIBIT No. 280

Received in evidence, June 3, 1941, Tr. 2377, M. S. Jameson

The Denver and Rio Grande Western Railroad Company
The Denver and Salt Lake Western Railroad Company

Status of Indebtedness Owing to RFC as of January 1, 1941

Date of Note	Date of Maturity	Principal Balance	Rate of Interest	Date from which interest Computed	Interest Accrued and unpaid as of 1/1/41
3/29/32	3/29/35	$250,000.00	6%	4/ 1/40	$11,301.36
6/27/32	3/29/35	750,000.00	6%	12/27/39	45,739.74
7/29/32	3/29/35	1,000,000.00	6%	1/29/40	55,561.63
1/12/33	1/12/36	105,500.00	5%	7/12/35	28,904.05
2/ 2/33	2/ 2/36	91,800.00	5%	8/ 2/35	24,886.65
2/25/33	2/25/36	81,500.00	5%	8/25/35	21,837.57
3/22/33	3/22/36	88,800.00	5%	9/22/35	23,452.96
4/20/33	4/20/36	219,700.00	5%	10/ 1/35	57,754.01
4/25/33	Demand	1,000,000.00	6%	4/25/40	71,260.30
5/20/33	5/20/36	286,800.00	5%	5/ 1/35	81,404.08
6/26/33	6/26/36	231,900.00	5%	6/ 1/35	64,836.68
6/30/33	Demand	950,000.00	6%	5/18/38	149,689.38
7/20/33	7/20/36	197,600.00	5%	7/ 1/35	54,434.71
8/22/33	8/22/36	281,800.00	5%	8/ 1/35	76,433.37
9/22/33	9/22/36	472,000.00	5%	9/ 1/35	126,017.55
10/20/33	10/20/36	357,700.00	5%	10/ 1/35	94,031.00
11/20/33	11/20/36	201,600.00	5%	5/ 1/35	57,221.23
12/21/33	12/21/36	189,800.00	5%	6/ 1/35	53,066.00
1/16/34	1/16/37	163,500.00	5%	7/ 1/35	45,040.96
3/21/34	3/21/37	85,800.00	5%	9/1 /35	22,907.45
2/21/34	2/21/37	91,200.00	5%	8/ 1/35	24,736.43
4/30/34	4/30/37	115,300.00	5%	10/ 1/35	30,309.71
6/11/34	6/11/37	165,700.00	5%	6/ 1/35	46,327.93
6/26/34	6/26/37	99,000.00	5%	6/ 1/33	27,679.31
8/ 6/34	8/ 6/37	57,500.00	5%	8/ 1/35	15,595.89
8/31/34	8/31/37	46,500.00	5%	8/ 1/35	12,612.41
12/19/34	Demand	3,110,850.00	5%	6/ 3/35	868,891.67
	Total	$10,691,850.00			$2,161,934.05

Source of and Payments Received Since Date of Bankruptcy and Applied in Reduction of Accrued and Unpaid Interest

Payment received upon release of 3651 shares Capital Stock of The Denver & Salt Lake Railway Company	$700,000.00
Interest received on $1,266,000 The Denver & Salt Lake Railway Company Income Mortgage Bonds	275,355.00
Cash Dividend received on Capital Stock Rio Grande Motor Way, Inc.	62.50
Total	$975,417.50

Since January 1, 1941, $50,640.00 additional has been received representing interest on $1,266,000 The Denver & Salt Lake Railway Company Income Mortgage Bonds. This amount has also been applied in reduction of accrued and unpaid interest.

[fols. 1567-1568] At a Session of the Interstate Commerce Commission, Division 4, Held at Its Office in Washington, D. C., on the 8th Day of August, A. D. 1936.

Finance Docket No. 11002

Denver & Rio Grande Western Railroad Company
Reorganization

ORDER

It appearing, That the Bureau of Accounts of the Commission has prepared, by the direction of Division 4, a report dated July 29, 1936, on its investigation of the income accounts of The Denver and Rio Grande Western Railroad Company, debtor, and its subsidiaries, for the calendar years 1930 to 1934, inclusive, and that, pursuant to the provisions of Section 77 (c) (11) of the act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States", as amended, the Commission may direct said bureau to file such report in the proceeding pending before the Commission for the reorganization of said debtor, Finance Docket No. 11002;

It is ordered, That said report be filed in, and made a part of, the record in said proceeding.

By the Commission, division 4.

George B. McGinty, Secretary. (Seal.)

[fol. 1569] INTERSTATE COMMERCE COMMISSION

Bureau of Accounts—D. C. 9550—X (h)

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company

Accounting Investigation of Net Income for Years 1930-1934, Inclusive. Submitted July 29, 1936

Interstate Commerce Commission, Bureau of Accounts

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company Reorganization

In the matter of The Denver and Rio Grande Western Railroad Company, Debtor. In the proceedings for the reorganization of a railroad.

Report concerning income of The Denver and Rio Grande Western Railroad Company and its subsidiaries, for the five years ended December 31, 1930, to December 31, 1934, inclusive.

Filed in these proceedings by direction of the Interstate Commerce Commission, Division 4, pursuant to paragraph (11) of subsection (c) of section 77 of the Act of July 1, 1898, entitled "An Act to establish a uniform system of bankruptcy throughout the United States, as amended," August 6, 1936.

[fol. 1570] INTERSTATE COMMERCE COMMISSION

Bureau of Accounts

This bureau has investigated the income accounts of The Denver and Rio Grande Western Railroad Company and its subsidiaries, The Denver and Salt Lake Western Railroad Company, the Goshen Valley Railroad Company, and, the Rio Grande Junction Railway Company, as stated on their books of account for the five years ended December 31, 1930-1934 for the purpose of determining whether they have been maintained in conformity with the accounting regulations prescribed by the Commission.

In conducting the investigation the accounts were analyzed with a view to determining that no amounts were included

as a debit or credit to income, which properly should have been included in other accounts, and that no amounts properly includible in income accounts were omitted. If any such were found, exceptions were prepared setting forth in detail the particulars in which the accounting as performed was at variance with the Commission's accounting regulations and indicating the amount by which the account was under or overstated as the result of the improper accounting. The only accounting exceptions necessary were in connection with the accounts of the parent company, The Denver and Rio Grande Western Railroad Company. Such exceptions were discussed with the carrier's accounting officer, to whom copies of the exceptions were furnished. [fol. 1571] The carrier is therefore in possession of full information concerning all exceptions taken.

The Denver and Rio Grande Western Railroad Company is the operating carrier of the group and the following particulars affect only the accounts of that carrier.

The Commission, as provided in its accounting regulations, upon application supported by a proper showing that inclusion in the appropriate operating accounts of certain items would produce a distortive showing, has at times authorized the carrier to enter the amounts in profit and loss accounts direct without passing them through the designated income accounts. In order to reflect the income which would have been shown on the carrier's books if such special permission had not been granted, exceptions have been prepared which have the effect, for the purpose of this investigation, of including all income items in the income accounts.

The Commission's order prescribing the rates and accounting procedure which must be observed by carriers in accounting for depreciation of equipment, became effective January 1, 1935. This order as well as certain legislative enactments passed subsequent to December, 1934, will necessitate charges to income for depreciation and taxes in future years which were not required during the period covered by the bureau's investigation. The legislation referred to is the social security act approved August 14, 1935, and the railroad retirement act and related excise tax act approved [fol. 1572] August 29, 1935, which impose additional taxes upon carriers.

In order to indicate the effect on income had such order and legislation been in effect during the five years ended

December 31, 1934, exceptions have been prepared to show the amount of adjustments that would be required in the income accounts as stated for such period.

As these exceptions are intended as informative only, and merely as an indication of the possible effect such order and legislation would have had upon the prior years' income, in view of the difficulty and length of time required to determine with exactness the adjustments that would be necessary, the amounts thereof were estimated as indicated hereinafter.

During the five-year period, under the Commission's accounting regulations, the carrier determined from its own experience the rates at which charges were made to operating expenses for depreciation of the several classes of equipment. Such rates were determined for each unit of equipment and were applied until there had been charged to operating expenses and credited to the depreciation reserve an amount equal to the service loss (ledger value less salvage) after which no further depreciation charges were made. Upon retirement of the unit there was charged to the depreciation reserve the amount standing therein with respect to the unit, and if the equipment was retired before completion of its expected life, the difference between the [fol. 1573] service loss and the amount in the depreciation reserve was charged to operating expenses at the time of retirement.

Under the Commission's order, effective January 1, 1935, the rates to be charged for depreciation are prescribed by the Commission. Such charges are to be continued during the entire life of the equipment and at time of retirement of a unit the entire service loss is charged to the depreciation reserve.

In determining the adjustment that should be made for the purpose of arriving at the income for the five-year period ended December 31, 1934, had the depreciation order been effective during such period, the depreciation charges on equipment in service during the five-year period were computed on the basis of rates prescribed by the Commission. From the amounts of such recomputed depreciation were deducted the depreciation charges actually entered in the accounts plus charges made to operating expenses for service loss on retired equipment together with similar items included in profit and loss accounts by permission of

the Commission which have been restored to income through exceptions previously described.

Section 901, Title IX, of the social security act, approved August 14, 1935, effective January 1, 1936, provides for an excise tax at the rate of 1 per cent for the year 1936, 2 per cent for the year 1937 and 3 per cent thereafter, applied to the total wages payable. In view of the uncertainty of the effective date of the reorganization of the carrier, the maxi-
[fol. 1574] mum rate of 3 per cent was applied to the total pay rolls for each of the years 1930 to 1934 in computing the amount of tax which would have been chargeable to income if the social security act had been in effect during those years.

Under the retirement act approved June 27, 1934, the carrier set up charges for contributions to a retirement fund at the rate of 4 per cent of the compensation not in excess of $300 per month paid its employees. This act was held unconstitutional by the Supreme Court May 6, 1935, and a new act which was approved August 29, 1935 provided for the payment of a tax at the rate of 3½ per cent of the compensation not in excess of $300 per month paid its employees. The ratio of the aggregate of the amounts which the carrier had determined to be payable under the invalidated railroad retirement act to the total pay rolls of the periods to which the amounts payable applied was determined. This ratio was reduced one eighth to adjust for the difference between the rates of 4 per cent and 3½ per cent as provided in the respective acts. The reduced ratio so determined was applied to the total monthly pay rolls for the five-year period and from the result were deducted the amounts charged operating expenses for pensions during those five years. The results so determined are considered to be the additional amounts that would have been charged to income during that period had the present retirement act been then in effect.

The results of this Bureau's investigation of the carrier's
[fol. 1575] accounts are shown on the statement submitted herewith identified as "Schedule 1". The statement consists of a summary of the income accounts as stated on the carrier's books of account for each of the five years ended December 31, 1930-1934, total for the period and the yearly average.

The statement also shows the amounts of income available for the payment of interest as reflected by the carrier's

books; as corrected to eliminate accounting errors; as adjusted to include income items entered in profit and loss accounts by permission of the Commission; and as further adjusted to give retroactive effect to new legislation and revised accounting regulations. The statement further shows the correction necessary in the accounts for interest payments in order to state those accounts in conformity with the Commission's accounting regulations and to include therein amounts charged to profit and loss by permission of the Commission. Details of the adjustments are shown on a supplemental statement, identified as "Schedule 1-A".

With respect to the subsidiaries there are submitted herewith statements showing information relating thereto identified as follows:

Company	Schedule
The Denver and Salt Lake Western Railroad Company	2
Goshen Valley Railroad Company	3
The Rio Grande Junction Railway Company	4

(Here fololw 2 pasters, side folios 1576, 1577)

[fol. 1576]

SCHEDULE 1

Interstate Commerce Commission

Bureau of Accounts

The Denver and Rio Grande Western Railroad Company

Statement of net income, or deficit, for the five years from 1930 to 1934, inclusive

	Year 1930	1931	1932	1933	1934	Five year Total	Average per year
As stated on the carrier's books of account:							
Net railway operating income	$6,940,932 29	$5,137,991 16	$2,814,269 15	$3,357,643 36	$2,311,563 88	$20,562,409 84	$4,112,481 97
Other income	298,858 30	186,223 96	200,797 23	160,988 39	484,518 24	1,331,386 12	266,277 22
Total income	$7,239,800 59	$5,324,215 12	$3,015,066 38	$3,518,631 75	$2,796,082 12	$21,893,795 96	$4,378,759 19
Miscellaneous deductions from income	17,947 70	17,517 35	18,293 24	17,642 86	14,870 97	86,272 12	17,254 42
Income available for fixed charges	$7,221,852 89	$5,306,697 77	$2,996,773 14	$3,500,988 89	$2,781,211 15	$21,807,523 84	$4,361,504 77
Fixed charges other than interest	102,194 12	102,194 12	102,194 12	102,194 12	180,933 19	589,709 67	117,941 93
Income available for payment of interest	$7,119,658 77	$5,204,503 65	$2,894,579 02	$3,398,794 77	$2,600,277 96	$21,217,814 17	$4,243,562 84
Interest on funded debt	$5,384,335 83	$5,368,317 83	$5,324,008 84	$5,381,398 41	$5,394,588 87	$26,852,649 78	$5,370,529 96
Interest on unfunded debt	51,041 50	61,837 78	154,780 20	156,349 44	181,560 84	605,569 76	121,113 95
Total interest	$5,435,377 33	$5,430,155 61	$5,478,789 04	$5,537,747 85	$5,576,149 71	$27,458,219 54	$5,491,643 91
Total net income	$1,684,281 44	$225,651 96D	$2,584,210 02D	$2,138,953 08D	$2,975,871 75D	$6,240,305 37D	$1,248,081 07D
Income available for payment of interest:							
As shown by carrier's books of account	$7,119,658 77	$5,204,503 65	$2,894,579 02	$3,398,794 77	$2,600,277 96	$21,217,814 17	$4,243,562 84
After correcting accounting not in conformity with the Commission's accounting regulations	6,643,686 30	5,212,094 88	2,884,206 83	3,356,210 17	2,494,674 77	20,590,872 95	4,118,174 59
After adjustment to include income items entered in profit and loss account by permission of the Commission	6,643,686 30	5,212,094 88	2,884,206 83	3,356,210 17	2,118,353 44	20,214,551 62	4,042,910 32
After further adjustment to give retroactive effect to (a) new legislation and to (b) current regulations governing accounting for depreciation of equipment	5,731,177 57	4,532,363 10	2,370,290 19	2,883,485 04	2,088,477 58	17,606,193 48	3,521,238 70
Interest on unfunded debt after correcting accounting not in conformity with the Commission's accounting regulations	$51,041 50	$186,928 57	$185,313 55	$173,391 80	$187,191 81	$783,867 23	$156,773 45
Interest on unfunded debt after adjustment to include items entered in profit and loss account by permission of the Commission	51,041 50	186,928 57	185,313 55	173,391 80	370,070 47	966,745 89	193,349 18

D—Denotes deficit in income.

[fol. 1577]

Interstate Commerce Commission

Bureau of Accounts

The Denver and Rio Grande Western Railroad Company

Detail of modification of income resulting from investigation of the carrier's accounts

Schedule 1-A

	Primary account affected	All modifications have the effect of increasing income unless indicated by symbol "*" Year 1930	1931	1932	1933	1934
Net income available for payment of interest as stated on the carrier's books of account		$7,119,658.77	$5,204,503.65	$2,894,579.02	$3,398,794.77	$2,600,277.96
Modifications necessary to correct accounting not in conformity with the Commission's regulations:						
Exception No. 1—Service loss on property retired and replaced charged to profit and loss	531	334,972.47*	42,286.37*	421.06*	42,584.60*	86,875.73*
Exception No. 2—Interest received on tax refunds credited to profit and loss	515		49,877.60			
Exception No. 3—Profit derived from exchange of stock accounted for as dividend	513	16,000.00*				
Exception No. 4—Reparation claim payments charged to profit and loss	501					9,455.84*
Exception No. 5—Advance accounting for renewal of cross ties	531	125,000.00*				
Exception No. 6—Payment for pickup and delivery service charged to profit and loss	501					9,271.62*
Exception No. 7—Adjustment of accounts receivable through profit and loss instead of account originally credited	501			181.38*		
	504			1,206.00*		
	531			2,935.55*		
	536			52.00*		
Exception No. 8—Offset settlement applied to accounts previously charged instead of accounts receivable	501			1,019.47*		
	504			540.00*		
	507			640.25*		
	510			352.51*		
	531			3,023.97*		
Net income available for payment of interest after modification to correct accounting not in conformity with the Commission's accounting regulations		$6,643,686.30	$5,212,094.88	$2,884,206.83	$3,356,210.17	$2,494,674.77
Modifications to include items entered in profit and loss by permission of the Commission which in the absence of such permission would be includible in income accounts:						
Exception No. A-2—Retirement of obsolet equipment	531					376,321.33*
Net income available for payment of interest after adjustment to include income items entered in profit and loss by permission of the commission		$6,643,686.30	$5,212,094.88	$2,884,206.83	$3,356,210.17	$2,118,353.44
Modifications to give retroactive effect to new legislation and to current accounting regulations as indicated below:						
Exception No. A-4—Railroad retirement act and related excise tax act effective March 1, 1935	531	167,663.74	197,963.27	177,653.72	180,329.73	352,858.18
	532	504,988.50*	385,433.61*	289,755.93*	270,039.03*	319,054.82*
Exception No. A-5—Social Security Act effective January 1, 1936	532	444,401.73*	339,190.62*	254,992.02*	237,640.68*	280,775.73*
Exception No. A-1—Commission's order respecting accounting for equipment depreciation effective January 1, 1935	531	130,482.24*	153,070.82*	146,722.41*	145,375.15*	217,096.51
Net income available for payment of interest after further adjustment to give retroactive effect to new legislation and to current accounting regulations regarding equipment depreciation		$5,731,477.57	$4,532,363.10	$2,370,390.19	$2,883,485.04	$2,088,477.58
Interest on unfunded debt as stated on carrier's books of account		$51,041.50	$61,837.78	$154,780.20	$156,349.44	$181,560.84
Modifications necessary to correct accounting not in conformity with the Commission's regulations:						
Exception No. 2—Interest on additional tax assessments charged to profit and loss	547		81,673.94*			
Exception No. 4—Interest on reparation claims charged to profit and loss	547		43,416.85*	30,533.35*	17,042.36*	5,630.97*
Interest on unfunded debt after modification to correct accounting not in conformity with the Commission's accounting regulations		$51,041.50	$186,928.57	$185,313.55	$173,391.80	$187,191.81
Modifications to include items entered in profit and loss by permission of the Commission which in the absence of such permission would be includible in income accounts:						
Exception No. A-3—Interest paid on special assessments	547					182,878.66*
Interest on unfunded debt after adjustment to include income items entered in profit and loss by permission of the Commission		$51,041.50	$186,928.57	$185,313.55	$173,391.80	$370,070.47

[fol. 1578] Schedule 2

Interstate Commerce Commission

Bureau of Accounts

The Denver and Salt Lake Western Railroad Company

This company was incorporated for the purpose of constructing a line of railroad from Bond to Dotsero, Colorado. Construction was completed in June 1934 and the property was leased to The Denver and Rio Grande Western Railroad Company effective June 15, 1934.

The company has no net income, the lessee being required to assume all charges and pay rental equal to dividends on capital stock, which for the period from June 15 to December 31, 1934, amounted to $78,739.07. The dividend accrued on capital stock owned by the lessee and pledged as collateral for loans by the Reconstruction Finance Corporation to the lessee. Under the loan agreement, the payment of dividends on the pledged stock equal to interest on the loans unpaid is guaranteed jointly by the lessor and lessee.

[fol. 1579] Schedule 3

Interstate Commerce Commission

Bureau of Accounts

Goshen Valley Railroad Company

The property of this company is leased to The Denver and Rio Grande Western Railroad Company which owns all the company's outstanding capital stock.

No net income is shown by the company's books of account. For each of the five years 1930-1934 there was recorded $1 for rental received and a like amount for dividend appropriation.

[fol. 1580] Schedule 4

Interstate Commerce Commission

Bureau of Accounts

The Rio Grande Junction Railway Company

The property of this company is leased and forms that part of the main line of The Denver and Rio Grande West-

ern Railroad Company from Rifle Creek to Grand Junction, Colorado.

For each of the five years 1930-1934 the books of account show a rental income of $100,000 and a charge of the same amount for interest on funded debt. In addition to the rental and interest items for the five years there are shown the following items resulting in a net deficit of $3,232.17 for the five year period:

	(Account 515)	(Account 549)	(Account 551)	
Year	Interest Received	Expenses	Taxes*	Net Deficit
1930	$173.55	$ 3.62	$ 628.89	$ 458.96
1931	101.21	103.80	527.75	530.34
1932	61.54	102.50	647.50	688.46
1933	24.03	221.30	608.00	805.27
1934		105.06	644.08	749.14
	$360.33	$536.28	$3,056.22	$3,232.17

*Normal income tax, on interest on tax free bonds.

No adjustment of the foregoing is necessary as a result of investigation of the company's accounts.

[fol. 1580a] At a Session of the Interstate Commerce Commission, Division 4, held at its office in Washington, D. C., on the 9th day of January, A. D., 1937

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company
Reorganization

ORDER

It appearing, That the Bureau of Accounts of the Commission has prepared, by the direction of Division 4, a report dated December 22, 1936, on its investigation of the income accounts of The Denver and Salt Lake Railway Company, one of the railroad companies embraced in the plan of consolidation and reorganization of The Denver and Rio Grande Western Railroad Company, debtor, for the calendar years 1930 to 1934, inclusive, and that, pursuant to the provisions of Section 77 (c) (11) of the act of

July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States", as amended, the Commission may direct said bureau to file such report in the proceeding pending before the Commission for the reorganization of the said debtor, Finance Docket No. 11002;

[fol. 1580b] *It is ordered*, That said report be filed in, and made a part of, the record in said proceeding.

By the Commission, division 4.

George B. McGinty, Secretary. (Seal.)

Interstate Commerce Commission

Bureau of Accounts—D.C. 9550-X(s)

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company

Accounting Investigation of Net Income of

The Denver and Salt Lake Railway Company

for Years 1930-1934, inclusive

Submitted December 22, 1936

Interstate Commerce Commission

Bureau of Accounts

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company
Reorganization

In the matter of The Denver and Rio Grande Western Railroad Company, Debtor. In proceedings for the reorganization of a railroad.

[fol. 1580c] Report concerning income of The Denver and Salt Lake Railway Company for the five years ended December 31, 1930, to December 31, 1934, inclusive.

Filed in these proceedings by direction of the Interstate Commerce Commission, Division 4, pursuant to paragraph (11) of subsection (c) of section 77 of the Act of July 1, 1898, entitled "An Act to establish a uniform system of bankruptcy throughout the United States, as amended."

January 9, 1937.

Interstate Commerce Commission

Bureau of Accounts

This bureau has investigated the income accounts of The Denver and Salt Lake Railway Company as stated on the books of account for the five years ended December 31, 1930-1934, for the purpose of determining whether they have been maintained in conformity with the accounting regulations prescribed by the Commission.

In conducting the investigation the accounts were analyzed with a view to determining that no amounts were included as a debit or credit to income, which properly should have been included in other accounts, and that no amounts properly includible in income accounts were omitted. If any such were found, exceptions were prepared setting forth in detail the particulars in which the accounting as performed was at variance with the Commission's accounting regulations and indicating the amount by which [fol. 1580d] the account was under or overstated as the result of the improper accounting. Such exceptions have been presented to the carrier's accounting officer, who is therefore in possession of full information concerning all exceptions taken.

The Commission, as provided in its accounting regulations, upon application supported by a proper showing that inclusion in the appropriate operating accounts of certain items would produce a distortive showing, has at times authorized the carrier to enter the amounts in profit and loss accounts direct without passing them through the designated income accounts. In order to reflect the income which would have been shown on the carrier's books if such special permission had not been granted, exceptions have been prepared which have the effect, for the purpose of this investigation, of including all income items in the income accounts.

The Commission's order prescribing the rates and accounting procedure which must be observed by carriers in accounting for depreciation of equipment, became effective January 1, 1935. This order as well as certain legislative enactments passed subsequent to December, 1934, will necessitate charges to income for depreciation and taxes in future years which were not required during the period covered by the bureau's investigation. The legislation referred to

is the social security act approved August 14, 1935, and the railroad retirement act and related excise tax act approved August 29, 1935, which impose additional taxes upon carriers.

[fol. 1580e] In order to indicate the effect on income had such order and legislation been in effect during the five years ended December 31, 1934, exceptions have been prepared to show the amount of adjustments that would be required in the income accounts as stated for such period.

As these exceptions are intended as informative only, and merely as an indication of the possible effect such order and legislation would have had upon the prior years' income, in view of the difficulty and length of time required to determine with exactness the adjustments that would be necessary, the amounts thereof were estimated as indicated hereinafter.

During the five-year period, under the Commission's accounting regulations, the carrier determined from its own experience the rates at which charges were made to operating expenses for depreciation of the several classes of equipment. Such rates were determined for each unit of equipment and were applied until there had been charged to operating expenses and credited to the depreciation reserve an amount equal to the service loss (ledger value less salvage) after which no further depreciation charges were made. Upon retirement of the unit, there was charged to the depreciation reserve the amount standing therein with respect to the unit, and if the equipment was retired before completion of its expected life, the difference between the service loss and the amount in the depreciation reserve was [fol. 1580f] charged to operating expenses at the time of retirement.

Under the Commission's order, effective January 1, 1935, the rates to be charged for depreciation are prescribed by the Commission. Such charges are to be continued during the entire life of the equipment and at time of retirement of a unit the entire service loss is charged to the depreciation reserve.

In determining the adjustment that should be made for the purpose of arriving at the income for the five-year period ended December 31, 1934, had the depreciation order been effective during such period, the depreciation charges on equipment in service during the five-year period were

computed on the basis of rates prescribed by the Commission. From the amounts of such recomputed depreciation were deducted the depreciation charges actually entered in the accounts plus charges made to operating expenses for service loss on retired equipment together with similar items included in profit and loss accounts by permission of the Commission which have been restored to income through exceptions previously described.

Section 901, Title IX, of the social security act, approved August 14, 1935, effective January 1, 1936, provides for an excise tax at the rate of 1 per cent for the year 1936, 2 per cent for the year 1937 and 3 per cent thereafter, applied to the total wages payable. In view of the uncertainty of the effective date of the reorganization of the carrier, the maxi-[fol. 1580g] mum rate of 3 per cent was applied to the total pay rolls for each of the years 1930 to 1934, in computing the amount of tax which would have been chargeable to income if the social security act had been in effect during those years.

Under the retirement act approved June 27, 1934, the carrier set up charges for contributions to a retirement fund at the rate of 4 per cent of the compensation not in excess of $300 per month paid employees. This act was held unconstitutional by the Supreme Court May 6, 1935, and a new act which was approved August 29, 1935, provided for the payment of a tax at the rate of 3½ per cent of the compensation not in excess of $300 per month paid employees. The ratio of the aggregate of the amounts which the carriers had determined to be payable under the invalidated railroad retirement act to the total pay rolls of the periods to which the amounts payable applied was determined. This ratio was reduced one-eighth to adjust for the difference between the rates of 4 per cent and 3½ per cent as provided in the respective acts. The reduced ratio so determined was applied to the total monthly pay rolls for the five-year period and from the result were deducted the amounts charged operating expenses for pensions during those five years. The results so determined are considered to be the additional amounts that would have been charged to income during that period had the present retirement act been then in effect.

The results of this bureau's investigation of the carrier's [fol. 1580h] accounts are shown on the statement submitted

herewith identified as "Schedule 1". The statement consists of a summary of the income accounts as stated on the carrier's books of account for each of the five years ended December 31, 1930-1934, total for the period and the yearly average. The statement also shows the amounts of income available for the payment of interest as reflected by the carrier's books; as corrected to eliminate accounting errors; as adjusted to include income items entered in profit and loss accounts by permission of the Commission; and, as further adjusted to give retroactive effect to new legislation and revised accounting regulations, and the correction required in the accounts for interest payments in order to state those accounts in conformity with the Commission's accounting regulations. Details of the adjustments are shown on supplemental statement identified as "Schedule 1-A."

[fol. 1580-i]

Interstate Commerce Commission

Bureau of Accounts

The Denver and Salt Lake Railway Company

Statement of net income, or deficit, for the five years from 1930 to 1934, inclusive

Schedule 1

	Year					Five year total	Average per year
	1930	1931	1932	1933	1934		
As stated on the carrier's books of account:							
Net railway operating income	$1,123,752.78	$859,358.60	$812,424.67	$711,348.02	$913,122.28	$4,420,006.35	$884,001.27
Other income	140,428.13	386,680.65	161,712.09	133,979.54	99,829.99	922,630.40	184,526.08
Total income	$1,264,180.91	$1,246,039.25	$974,136.76	$845,327.56	$1,012,952.27	$5,342,636.75	$1,068,527.35
Miscellaneous deductions from income	11,220.57	9,315.32	10,664.23	9,542.99	7,618.67	48,361.78	9,672.36
Income available for fixed charges	$1,252,960.34	$1,236,723.93	$963,472.53	$835,784.57	$1,005,333.60	$5,294,274.97	$1,058,854.99
Fixed charges other than interest	411,631.93	400,747.94	397,019.86	403,278.43	402,743.46	2,015,421.62	403,084.32
Income available for payment of interest	$841,328.41	$835,975.99	$566,452.67	$432,506.14	$602,590.14	$3,278,853.35	$655,770.67
Interest on funded debt—(a) Fixed interest	$810,000.00	$810,000.00	$562,500.00	$425,000.00	$590,000.00	$3,197,500.00	$639,500.00
Interest on unfunded debt	1,081.05	572.12	6.51	3,359.82	96.54	5,116.04	1,023.21
Total interest	$811,081.05	$810,572.12	$562,506.51	$428,359.82	$590,096.54	$3,202,616.04	$640,523.21
Total net income	$30,247.36	$25,403.87	$3,946.16	$4,146.32	$12,493.60	$76,237.31	$15,247.46
Income available for payment of interest:							
As shown by carrier's books of account	$841,328.41	$835,975.99	$566,452.67	$432,506.14	$602,590.14	$3,278,853.35	$655,770.67
After correcting accounting not in conformity with the Commission's accounting regulations	858,594.69	838,949.01	551,281.24	433,530.66	535,443.60	3,217,799.20	643,559.84
After adjustment to include income items entered in profit and loss account by permission of the Commission	858,594.69	838,949.01	545,464.98	364,355.65	460,473.05	3,067,836.48	613,567.29
After further adjustment to give retroactive effect to (a) new legislation and to (b) current regulations governing accounting for depreciation of equipment	791,850.62	766,154.68	462,511.55	295,688.42	385,767.69	2,701,972.96	540,394.59
Interest on unfunded debt after adjustment to include income items entered in profit and loss account by permission of the Commission	$1,081.05	$24,500.43	$6.51	$3,359.82	$96.54	$29,044.35	$5,808.87

[fol. 1580-j]

Interstate Commerce Commission
Bureau of Accounts

The Denver and Salt Lake Railway Company
Detail of modification of income resulting from investigation of the carrier's account

Schedule 1-A

All modifications have the effect of increasing income unless indicated by symbol "*"

	Income account affected	Year 1930	1931	1932	1933	1934
Net income available for payment of interest as stated on the carrier's books of account		$841,328.41	$835,975.99	$566,452.67	$432,506.14	$602,590.14
Modifications necessary to correct accounting not in conformity with the Commission's regulations:						
Exception No. 1—Failure to account for estimated cost of bridges used in lieu of temporary trestles for purpose of filling	531	12,828.49	1,711.74	159.33	—	60,822.23*
Exception No. 2—Failure to inventory construction projects within reasonable time after completion thereof and make necessary adjustments	531	3,597.79	1,261.28	15,330.76**	1,024.52	5,484.31*
	504	840.00	—	—	—	840.00*
Net income available for payment of interest after modification to correct accounting not in conformity with the Commission's accounting regulations		$858,594.69	$838,949.01	$551,281.24	$433,530.66	$535,443.60
Modifications to include items entered in profit and loss by permission of the Commission which in the absence of such permission would be includible in income accounts:						
Exception No. A-1—Service loss on obsolete equipment retired	531	—	—	—	20,783.50*	19,192.44*
Exception No. A-2—Legal expenses in connection with Moffat Tunnel lease	531	—	—	—	17,500.00*	—
Exception No. A-3—Rental on Moffat Tunnel paid under judgment of District Court	542	—	—	5,817.46*	—	—
Exception No. A-8—Loss on timber lining of Moffat Tunnel retired	531	—	—	—	30,891.42*	55,778.11*
Net income available for payment of interest after adjustment to include income items entered in profit and loss by permission of the Commission		$858,594.69	$838,949.01	$545,464.08	$364,355.65	$460,473.05
Modifications to give retroactive effect to new legislation and to current accounting regulations as indicated below:						
Exception No. A-4—Railroad retirement act and related excise tax act effective March 1, 1936	532	46,363.56*	29,620.46*	24,241.28*	25,615.43*	26,869.48*
Exception No. A-6—Social security act effective January 1, 1936	532	41,136.48*	26,281.02*	21,508.29*	22,727.52*	23,840.19*
Exception No. A-7—Commission's order respecting equipment depreciation accounting effective January 1, 1935	531	20,755.97	16,892.85*	37,202.96*	20,324.28*	23,995.69
Net income available for payment of interest after further adjustment to give retroactive effect to new legislation and to current accounting regulations regarding equipment depreciation		$791,850.62	$766,154.68	$462,511.55	$295,688.42	$385,767.69
Interest on unfunded debt as stated on carrier's books of account		$1,081.05	$572.12	$6.51	$3,359.82	$96.54
Modifications to include items entered in profit and loss by permission of the Commission which in the absence of such permission would be includible in income accounts:						
Exception No. A-5—Interest on delayed payment of State taxes	547	—	23,928.31*	—	—	—
Interest on unfunded debt after adjustment to include income items entered in profit and loss by permission of the Commission		$1,081.05	$24,500.43	$6.51	$3,359.82	$96.54

[fol. 1581] At a Session of the Interstate Commerce Commission, Division 4, held at its office in Washington, D. C., on the 8th day of March, A. D. 1937.

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company Reorganization

ORDER

It appearing, That the Bureau of Valuation of this Commission has prepared, by direction of Division 4, a report dated March 1, 1937, on its investigation of the elements of value, and related matters, of the properties of The Denver and Rio Grande Western Railroad Company, The Denver and Salt Lake Western Railroad Company, the Goshen Valley Railroad Company, The Rio Grande Junction Railway Company, The Denver and Salt Lake Railway Company, and the Moffat Tunnel Improvement District, as of December 31, 1935, and that pursuant to the provisions of section 77 (c) (11) of the Act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States", as amended, the Commission may direct said bureau to file such a report in the proceedings pending before it for the reorganization of said debtors;

[fol. 1582] *It is ordered*, That said report be filed in, and made a part of the record of this proceeding.

By the Commission, division 4.

George W. Laird, Acting Secretary. (Seal.)

[fol. 1583] Denver and Rio Grande Western Railroad Company, Denver and Salt Lake Western R. R. Co., Goshen Valley R. R. Co., Rio Grande Junction Ry. Co.

Denver and Salt Lake Railway Company, Moffat Tunnel Improvement District

Report of the Bureau of Valuation on the following matters as of December 31, 1935

Mileage.
Elements of value of property owned.
Elements of value of property underlying mortgages.

Investment in physical property and in securities of carrier and noncarrier corporations.
Summary of funded debt.
Capital stock and long-term debt outstanding.
Corporate history.
Development of fixed physical property.
History of corporate financing:

March 1, 1937.

[fol. 1584]

Denver and Rio Grande Western Railroad Company
Mileage as of December 31, 1935

	First main	Other main	Yard tracks and sidings	All tracks
Denver and Rio Grande Western R. R.				
Wholly owned and used:				

[fol. 1584]

Denver and Rio Grande Western Railroad Company

Mileage as of December 31, 1935

	First main	Other main	Yard tracks and sidings	All tracks
Denver and Rio Grande Western R. R.				
Wholly owned and used:				
Standard gauge	1,562.292	146.536	794.340	2,503.168
Narrow gauge	735.408	.....	85.263	820.671
Three rail	58.682	3.861	42.741	105.284
Four rail	.....	.....	0.580	0.580
Total wholly owned and used	2,356.382	150.397	922.924	3,429.703
Jointly owned and used:				
Standard gauge	1.472	0.506	21.588	23.566
Three rail	0.260	.....	0.278	0.538
Total jointly owned and used	1.732	0.506	21.866	24.104
Wholly used but not owned:				
Standard gauge	110.576	0.456	38.038	149.070
Narrow gauge	36.040	.....	6.026	42.066
Total wholly used but not owned	146.616	0.456	44.064	191.136
Jointly used but not owned:				
Standard gauge	0.716	.....	0.490	1.206
Narrow gauge	.....	.....	0.314	0.314
Total jointly used but not owned	0.716	.....	0.804	1.520
Total wholly owned	2,356.382	150.397	922.924	3,429.703
Total jointly owned	1.732	0.506	21.866	24.104
Total wholly used	2,502.998	150.853	966.988	3,620.839
Total jointly used	2.448	0.506	22.670	25.624

Note: In addition to the miles of track shown as wholly owned and used by the Denver and Rio Grande Western Railroad Company it also wholly owns and uses 1.501 miles of a third or single rail laid in the tracks of the New Mexico Central R. R. Co., over which it has trackage rights.

[fol. 1585]

Denver and Sale Lake Western R. R.				
Owned but not used	38.062	.....	14.619	52.681
Goshen Valley R. R.				
Owned but not used	9.272	0.456	1.738	11.466
Rio Grande Junction Ry.				
Owned but not used	62.075	.....	21.204	83.279
Denver and Salt Lake Ry.				
Wholly owned and used	220.355	.....	70.515	290.870
Wholly owned but not used	.....	.....	0.089	0.089
Wholly used but not owned	12.094	.....	4.734	16.828
Total owned	220.355	.....	70.604	290.959
Total used	232.449	.....	75.249	307.698
Moffat Tunnel Improvement Dist.				
Owned but not used	8.914	.....	1.972	10.886

[fol. 1586]

Denver and Rio Grande Western Railroad Company

Elements of Value as of December 31, 1935, of Property Owned

Denver and Rio Grande Western R. R.			
Original Cost			$142,800,512
Road		$104,308,393	
Equipment		38,492,119	
Cost of Reproduction New			168,729,747
Road		118,549,925	
Equipment		50,179,822	
Cost of Reproduction Less Depreciation			115,467,756
Road		94,535,747	
Equipment		20,932,009	
Value of Lands and Rights			5,428,159
Carrier		4,333,196	
Noncarrier		1,094,963	
Working Capital			2,473,400
Denver and Salt Lake Western R. R.			
Original Cost	Road		3,547,081
Cost of Reproduction New	Road		3,920,258
Cost of Reproduction Less Depreciation	Road		3,880,723
Value of Lands and Rights	Carrier		7,219
Goshen Valley R. R.			
Original Cost	Road		499,441
Cost of Reproduction New	Road		308,078
Cost of Reproduction Less Depreciation	Road		270,756
Value of Lands and Rights	Carrier		1,908

[fol. 1587]

Rio Grande Junction Ry.			
Original Cost	Road		$3,401,673
Cost of Reproduction New	Road		4,100,037
Cost of Reproduction Less Depreciation	Road		3,409,074
Value of Lands and Rights			60,330
Carrier		$54,006	
Noncarrier		6,324	
Denver and Salt Lake Ry.			
Original Cost			17,549,593
Road		14,502,554	
Equipment		3,047,039	
Cost of Reproduction New			19,934,420
Road		15,477,564	
Equipment		4,456,856	
Cost of Reproduction Less Depreciation			14,462,618
Road		13,204,327	
Equipment		1,258,291	
Value of Lands and Rights			91,854
Carrier		86,640	
Noncarrier		5,214	
Working Capital			287,000
Moffat Tunnel Improvement District (Owned by the State of Colorado)			
Original Cost			12,792,533
Cost of Reproduction New			8,813,873
Cost of Reproduction Less Depreciation			7,926,234
Value of Lands and Rights			596

[fol. 1588]

Denver and Rio Grande Western Railroad Company

Elements of Value as of December 31, 1935, of Property Owned

Original cost of property other than land has been determined in the following manner: For the Denver and Rio Grande Western Railroad and the Rio Grande Junction Railway by adding to the cost of reproduction new of road items as of date of basic valuation, based on 1910–1914 prices, and to the original cost of equipment (the Rio Grande Junction owns no equipment) as reported under Valuation Order No. 8, the cost of subsequent additions and retirements, as adjusted, ascertained from audited reports of the carriers under Valuation Order No. 3, form B. V. 588, through 1932 and from the carriers' records for 1933 to 1935, inclusive; for the Goshen Valley Railroad original cost as shown by the records; for the Denver and Salt Lake Western Railroad by adding to the original cost as of September 30, 1934, reported under Valuation Order No. 24, the cost of subsequent additions and retirements derived from the same sources as for the Denver and Rio Grande Western; for the Denver and Salt Lake Railway by adding to the cost of reproduction new of road items as of date of basic valuation, based on 1910–1914 prices, and to the original cost of equipment as reported under Valuation Order No. 8, the cost of subsequent additions and retirements, adjusted, ascertained from audited reports of the carrier under Valuation Order No. 3, form B. V. 588, through 1934 and from the carrier's records for 1935; and for the Moffat Tunnel Improvement District the original cost as shown by its records.

The amounts here reported for the Denver and Salt Lake Western Railroad, Goshen Valley Railroad and Moffat Tunnel Improvement District are the actual costs to December 31, 1935. For the Denver and Rio Grande Western Railroad the amount is 64.4 per cent actual and 35.6 per cent estimated, for the Rio Grande Junction Railway 68.3 per cent actual and 31.7 per cent estimated, and for the Denver and Salt Lake Railway 40.6 per cent actual and 59.4 per cent estimated.

Cost of reproduction new is based on revised inventories as of December 31, 1932, for the Denver and Rio Grande Western Railroad, Rio Grande Junction Railway and Goshen Valley Railroad, December 31, 1934 for the Denver and Salt Lake Railway and the Moffat Tunnel Improvement District and an inventory as of September 30, 1934, for the Denver

and Salt Lake Western Railroad with gross charges and credits for subsequent changes in property. Period prices were applied determined from consideration of records of prices and their individual trends prevailing in 1935 and during a period of time prior and subsequent thereto.

Cost of reproduction less depreciation has been determined in accordance with methods frequently explained in the Commission's printed valuation decisions.

[fol. 1589]

The value reported for lands is based on the application of unit values as of December 31, 1935, to detailed inventories as of December 31, 1932 for the Denver and Rio Grande Western Railroad, Rio Grande Junction Railway and Goshen Valley Railroad, December 31, 1934 for the Denver and Salt Lake Railway and Moffat Tunnel Improvement District, and an inventory of September 30, 1934 for the Denver and Salt Lake Western Railroad with adjustments estimated on the basis of cost for subsequent additions and retirements.

Working capital has been determined in accordance with the principles described in Northampton & B. R. Co., 159 I. C. C. 244, 263, under a simplified method applied in *Muskegon Ry. & Nav. Co.*, 45 Val. Rep. 797, and other valuation cases.

[fol. 1590] DEBTORS' EXHIBIT No. 1

The Denver and Rio Grande Western Railroad Company

Road Accounts			
Cost of Reproduction New (Units as of Dec. 31, 1932—Prices as of Dec. 31, 1938).			
Owned & Used			
Colorado	$86,575,726		
Utah	46,933,577		
New Mexico	5,553,539		
		139,062,842	
Jointly Owned & Used (D&RGW Portion)		116,777	
Jointly Owned & Wholly Used by D&RGW (D&RGW Portion)		38,510	
Unallocated (Acct. 37)		244,825	
Total		139,462,954	
Net Additions & Betterments to Road Accounts Jan. 1, 1933 to Dec. 31, 1938		927,028	
Total, Road Accounts, to Dec. 31, 1938		140,389,982	140,389,982
Lands			
Carrier	4,662,445		
Non Carrier	1,207,704		
		5,870,149	
Additions and Betterments to Land Acct. to Dec. 31, 1938	Cr.	24,390	
Total, Lands, to Dec. 31, 1938		5,845,759	5,845,759
Equipment			
Cost of Reproduction, Less Depreciation, as of Dec. 31, 1938			29,129,121
Total Cost of Reproduction Plus Value of Lands			$175,364,862

[fol. 1591] DEBTORS' EXHIBIT No. 5

Value of the Denver and Rio Grande Western Railroad Company, The Rio Grande Junction Railway Company, Goshen Valley Railroad Company, The Denver and Salt Lake Western Railroad Company

Cost of Reproduction New of Road Accounts, Cost of Reproduction Less Depreciation of Equipment, plus Value of Lands.		
The Denver and Rio Grande Western Railroad Company		$175,364,862
The Rio Grande Junction Railway Company		5,300,566
Goshen Valley Railroad Company		364,114
The Denver and Sale Lake Western Railroad Company		4,716,188
Total		$185,745,730
Additional Values		
Telegraph Lines	$300,000	
Water Rights	465,559	
Canon Rights	3,108,029	
Deficiency in Value of Narrow Gauge Equipment.	237,000	
		4,110,588
Additional Elements of Value		
Cost of Development of Property	9,000,000	
Going Concern Value	7,000,000	
Development of Business	550,000	16,550,000
Total Value as of December 31, 1938		$206,406,318

(Here follows 1 Photolithograph, side folio 1592)

In the matter of the Reorganization of
The Denver & Rio Grande Western Railroad Company, Debtor
Before the District Court of the United States
For the District of Colorado
Docket No. 8669

Exhibit 1
Witness

The Denver and Salt Lake Railway Company
Income Account
(000's Omitted)

	1927	1928	1929	1930	1931	1932	1933	1934	1935	1936	1937	1938	1939
Operating Revenues													
Freight	$3,546	$ 3,540	$ 3,471	$ 2,836	$ 2,038	$ 1,711	$ 1,470	$ 1,455	$ 2,075	$ 2,653	$ 2,602	$ 2,078	$ 2,114
Passenger	305	255	199	150	96	65	48	42	49	91	85	76	67
Mail	112	83	202	107	108	102	101	72	58	67	70	70	68
Express	49	48	40	54	24	13	9	12	9	9	10	7	6
All Other	98	86	69	70	42	24	29	39	44	37	39	33	36
Total	4,110	4,012	3,981	3,197	2,302	1,915	1,657	1,620	2,235	2,857	2,806	2,264	2,291
Operating Expenses													
Maintenance of Way and Structures	1,109	824	660	625	358	247	215	94	261	438	461	272	350
Maintenance of Equipment	1,218	903	785	642	395	294	276	251	424	711	655	458	489
Traffic	22	23	27	27	23	20	18	19	23	28	29	29	31
Transportation	919	688	610	514	396	321	302	333	515	722	811	693	710
General	122	129	164	181	131	116	120	134	116	116	118	123	111
Transportation for Investment - Cr.	14	31	19	15	-	19	42	16	62	76	52	5	-
Total	3,376	2,536	2,227	1,975	1,303	979	889	815	1,277	1,939	2,022	1,570	1,691
Operating Ratio	82.14	63.21	55.94	61.78	56.60	51.12	53.65	50.31	57.14	67.87	72.06	69.32	73.81
Net Revenue from Railway Operations	734	1,476	1,754	1,222	999	936	768	805	958	918	784	694	600
Railway Tax Accrual	88	132	156	185	200	163	167	167	180	270	317	353	350
Railway Operating Income	646	1,344	1,598	1,037	799	773	601	638	778	648	467	341	250
Equipment Rents - Net - Cr.	34	85	81	87	60	39	110	Dr. 5	Dr. 36	Dr. 97	Dr. 110	Dr. 48	Dr. 50
Joint Facility Rents - Net - Cr.	-	-	-	-	-	-	-	280	519	540	573	584	601
Net Railway Operating Income	680	1,429	1,679	1,124	859	812	711	913	1,261	1,091	930	877	801
Other Income	89	125	142	140	387	162	134	99	66	24	15	10	8
Total Income	769	1,554	1,821	1,264	1,246	974	845	1,012	1,327	1,115	945	887	809
Fixed Charges	142	502	551	574	561	557	566	560	577	508	523	501	477
Times Fixed Charges Earned	5.42	3.10	3.30	2.20	2.22	1.75	1.49	1.81	2.30	2.19	1.81	1.77	1.69
Balance Available for Interest on Income Bonds	627	1,052	1,270	690	685	417	279	452	750	607	422	386	332
Interest Actually Paid on Income Bonds	495	660	660	660	660	413	275	440	660	605	413	385	330
Per Cent Actually Paid on Income Bonds	4⅞%	6%	6%	6%	6%	3¾%	2½%	4%	6%	5½%	3¾%	3½%	3%
Balance after Interest Actually Paid on Income Bonds	132	392	610	30	25	4	4	12	90	2	9	1	2
Balance after 6% Interest on Income Bonds:													
Amount	D 33	392	610	30	25	D 243	D 381	D 208	90	D 53	D 239	D 274	D 328
Per Share on 50,000 shares no par Capital Stock	D 0.66	7.84	12.20	.60	.50	D 4.86	D 7.62	D 4.16	1.80	D 1.06	D 4.78	D 5.48	D 6.56

[fol. 1593] GUARANT. TRUST EX. No. 2

H. H. Copeland and Son Freight Traffic Density Statements for the Years Indicated:

(a) 1935
(b) 1936
(c) 1937
(d) 1938
(e) 1939

COURT EXHIBIT No. 2a

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Net Ton Miles
Revenue and Company
Year Ended December 31, 1935

Reads East		Net Ton Miles		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Alamo, Colo.	Walsenburg, Colo.	231,650	3,100	344,250	113,800
Alamosa, Colo.	La Veta, Colo.	194,033	120,262	528,574	455,967
Alamosa, Colo.	Mears Jct., Colo.	39,851	38,986	83,270	82,149
Antonito, Colo.	Alamosa, Colo.	106,276	52,483	233,069	176,862
Aspen, Colo.	Glenwood Springs, Colo.	19,951	9,488	50,854	40,390
Baldwin, Colo.	Gunnison, Colo.	36,833	611	54,500	18,056
Bingham, Utah	Midvale, Utah*	187,548	474,290	433,387	720,161
Bon Carbo, Colo.	Trinidad, Colo.	123,294	1,706	179,941	58,412
Bond—Orestod, Colo.	Denver, Colo.**	532,282	220,603	1,240,756	795,061
Capers, Colo.	Mustang, Colo.	5,500	—	9,000	3,000
Chama, N. M.	Antonito, Colo.	85,206	41,746	182,571	138,476
Clear Creek, Utah	Colton, Utah	35,857	1,381	56,381	22,000
Colorado Springs, Colo.	Denver, Colo.	579,397	230,849	1,201,329	985,644
Colton, Utah	Heiper, Utah	1,226,667	2,370,944	3,659,333	4,603,333
Creede, Colo.	Alamosa, Colo.	44,551	13,493	105,275	73,493
Crested Butte, Colo.	Gunnison, Colo.	205,071	3,607	295,107	93,536
Delta, Colo.	Montrose, Colo.	64,455	110,682	214,727	214,318
Detsero, Colo.	Bond-Orestod, Colo.	572,816	355,000	1,381,789	1,025,842
Dotsero, Colo.	Minturn, Colo.	810,241	625,586	2,025,466	1,760,069

Durango, Colo.	Chama, N. M.	59,741	34,333	133,861	107,759
Farmington, N. M.	Durango, Colo.	29,122	5,367	59,041	34,755
Glenwood Springs, Colo.	Dotsero, Colo.	1,374,853	996,253	3,365,799	2,803,180
Grand Jct., Colo.	Delta, Colo.	98,549	270,529	328,451	523,922
Grand Jct., Colo.	Glenwood Springs, Colo.	1,368,044	992,538	3,350,422	2,792,689
Green River, Utah	Utaline, Colo.	1,175,528	865,958	2,885,375	2,394,986
Gunnison, Colo.	Mears Jct., Colo.	238,603	12,714	362,524	136,968
Heber, Utah	Provo, Utah	19,308	18,192	54,538	52,615
Helper, Utah	Mounds, Utah	1,184,913	1,106,957	3,011,000	2,748,913
Kenilworth Jct., Utah	Kenilworth, Utah	Yard Movement		Yard Movement	
La Veta, Colo.	Walsenburg, Colo.	231,375	135,500	595,750	498,188
Manitou, Colo	Colorado Springs, Colo.	Yard Movement		Yard Movement	
Marysvale, Utah	Thistle, Utah	45,000	44,477	114,174	113,561
Mears Jct., Colo.	Poncha Jct., Colo.	273,333	51,167	441,000	216,833
Midvale, Utah	Provo, Utah	1,204,088	2,397,265	3,639,412	4,612,824
Minturn, Colo.	Salida, Colo.	769,908	468,747	1,921,655	1,562,954
Monarch, Colo.	Poncha Jct., Colo.	212,467	1,267	301,467	87,400
Montrose, Colo.	Gunnison, Colo.	17,645	12,694	43,871	39,323
Mounds, Utah	Green River, Utah	1,161,188	855,396	2,850,188	2,365,771
Nephi, Utah	Ephraim, Utah	13,310	4,643	26,833	19,333
Ogden, Utah	Salt Lake City, Utah	517,667	369,128	1,272,333	823,795
Ouray, Colo.	Montrose, Colo.	19,194	8,583	38,889	27,667
Pagosa Springs, Colo.	Pagosa Jct., Colo.	1,484	935	2,645	1,839
Park City, Utah	Roper, Utah	87,758	18,970	140,455	71,970
Poncha Jct., Colo.	Salida, Colo.	499,000	54,200	762,800	313,400
Provo, Utah	Springville, Utah	1,327,800	2,716,800	4,013,200	5,227,800
Pueblo, Colo.	Colorado Springs, Colo.	852,455	277,364	1,767,477	1,184,159
Rouse, Colo.	Rouse Jct., Colo.	89,000	1,875	133,000	39,875
Salida, Colo.	Pueblo, Colo.	1,180,052	456,646	2,537,865	1,753,365
Salt Lake City, Utah	Midvale, Utah	1,244,750	2,547,125	3,762,375	4,901,125
Santa Fe, N. M.	Antonito, Colo.	5,384	11,760	20,128	26,264
Silver City, Utah	Springville, Utah	958,222	21,200	241,244	102,689
Silverton, Colo.	Durango, Colo.	9,733	6,778	20,400	17,533
Soldier Summit, Utah	Colton, Utah	1,191,000	2,488,714	3,603,286	4,811,857
Somerset, Colo.	Delta, Colo.	261,721	10,372	408,349	152,651

COURT EXHIBIT No. 2a

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Net Ton Miles
Revenue and Company
Year Ended December 31, 1935

Reads East		Net Ton Miles		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Southern Jct., Colo.	Pueblo, Colo.	709,750	124,500	1,308,000	679,000
Spring Canyon Jct., Utah	Rains, Utah	Yard Movement		Yard Movement	
Springville, Utah	Thistle, Utah	1,180,267	2,415,000	3,567,267	4,647,000
Sunnyside, Utah	Mounds, Utah	223,353	2,294	324,941	103,000
Thistle, Utah	Soldier Summit, Utah	1,180,233	2,490,500	3,567,267	4,792,200
Trinidad, Colo.	Walsenburg, Colo.	296,396	69,104	489,479	270,208
Tropic, Colo.	La Veta, Colo.[1]	8,000	—	12,000	4,000
Utaline, Colo.	Grand Jct., Colo.	1,153,588	849,824	2,831,559	2,350,324
Walsenburg, Colo.	Southern Jct., Colo.	764,978	122,826	1,388,674	722,109
Westcliffe, Colo.	Texas Creek, Colo.	3,160	1,800	9,360	7,720
Grand Total—Denver & Rio Grande Western R. R.		414,623	317,167	987,217	846,878

(*) Also Garfield to Welby.
(**) Over Denver & Salt Lake Ry.
(#) Service Discontinued February 14, 1935.
(1) Service Discontinued February 28, 1935.

Rio Grande Southern R. R.

Durango, Colo.	Ridgway, Colo.	18,502 Both Directions.

[fol. 1595] COURT EXHIBIT No. 2a

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy. from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Net Ton Miles
Revenue and Company
Year Ended December 31, 1935

Mortgage Liens	Net Ton Miles (Revenue and Company) Density	Net Ton Miles (Revenue and Company) Per Dollar of Funded Debt Outstanding Including Prior Liens
Denver & Rio Grande R.R.—1st Const Mtge. 4s & 4½s, 1936	492,026	18
Rio Grande Western Ry.—1st Trust Mtge. 4s, 1939	1,939,965	53
Rio Grande Western Ry.—1st Cons. Mtge. 4s, 1949	1,203,906	27
Denver & Rio Grande Western R.R.—Rfdg. & Improv. Mtge. Series "A" 6s, 1974 and "B" 5s, 1978	722,902	18*
Denver & Rio Grande Western R.R.—Gen. Mtge. 5s, 1955	722,902	14*
Rio Grande Junction Ry.—1st Mtge. 5s, 1939	2,395,561	74
Rio Grande Southern R.R.—1st Mtge. 4s, 1940	18,502	1

* Direct and Collateral Lien.

Operated Mileage Discontinued During Year—Excluded.

Years Ended December 31	Net Ton Miles (Rev. & Co.) Density	Ratio of Revenue Ton Miles To Rev. & Company Ton Miles	Average Revenue Per Net Ton Mile Rev. & Co. Freight (Mills)	Density Per Cent of 1935
1935	731,790	90.8%	9.7	100.0%
1934	689,906	91.2	9.7	94.3

[fol. 15961]

COURT EXHIBIT No. 2b
The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Net Ton Miles
Revenue and Company
Year Ended December 31, 1936

Reads East		Net Ton Miles		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Alamo, Colo.	Walsenburg, Colo.	263,500	3,750	390,650	127,350
Alamosa, Colo.	La Veta, Colo.	328,607	159,328	851,066	668,016
Alamosa, Colo.	Mears Jct., Colo.	52,338	42,919	106,203	94,814
Antonito, Colo.	Alamosa, Colo.	158,172	71,172	328,000	234,586
Aspen, Colo.	Glenwood Springs, Colo.	34,098	8,829	86,390	60,585
Baldwin, Colo.	Gunnison, Colo.	39,944	1,222	58,833	20,555
Bingham, Utah	Midvale, Utah*	205,871	481,935	482,484	745,452
Bon Carbo, Colo.	Trinidad, Colo.	148,824	1,059	218,176	70,235
Bond—Orestod, Colo.	Denver, Colo.**	772,031	326,198	1,776,710	1,162,702
Capers, Colo.	Mustang, Colo.	9,500	500	12,500	5,500
Chama, N. M.	Antonito, Colo.	120,683	53,730	241,952	168,698
Clear Creek, Utah	Colton, Utah	41,905	1,810	65,476	28,143
Colorado Springs, Colo.	Denver, Colo.	769,986	291,288	1,545,507	1,175,425
Colton, Utah	Helper, Utah	1,612,667	2,740,444	4,495,778	5,471,889
Creede, Colo.	Alamosa, Colo.	66,739	13,725	165,348	111,319
Crested Butte, Colo.	Gunnison, Colo.	276,500	5,750	397,714	126,929
Delta, Colo.	Montrose, Colo.	72,500	152,864	283,045	303,500
Dotsero, Colo.	Bond—Orestod, Colo.	825,737	499,395	1,937,842	1,435,132
Dotsero, Colo.	Minturn, Colo.	1,062,483	857,241	2,506,103	2,315,000
Durango, Colo.	Chama, N. M.	79,639	42,444	165,157	125,546
Farmington, N. M.	Durango, Colo.	32,429	6,735	65,163	39,592

Glenwood Springs, Colo.	Dotsero, Colo.	1,882,316	1,343,797	4,408,159	3,695,611
Grand Jct., Colo.	Delta, Colo.	110,902	373,667	432,902	741,843
Grand Jct., Colo.	Glenwood Springs, Colo.	1,871,467	1,339,211	4,383,389	3,681,600
Green River, Utah	Utaline, Utah-Colo.	1,590,236	1,093,000	3,719,500	3,067,167
Gunnison, Colo.	Mears Jct., Colo.	310,825	18,984	465,048	172,651
Heber, Utah	Provo, Utah	19,038	29,154	66,885	76,885
Helper, Utah	Mounds, Utah	1,586,087	1,364,739	3,833,870	3,451,391
Kenilworth Jct., Utah	Kenilworth, Utah	Yard Movement		Yard Movement	
La Veta, Colo.	Walsenburg, Colo.	374,125	185,063	933,813	734,438
Manitou, Colo.	Colorado Springs, Colo.	Yard Movement		Yard Movement	
Marysvale, Utah	Thistle, Utah	54,917	52,712	141,659	137,788
Mears Jct., Colo.	Poncha Jct., Colo.	359,167	61,500	564,833	264,833
Midvale, Utah	Provo, Utah	1,594,853	2,772,618	4,532,529	5,491,942
Midvale, Utah	Sand Pit, Utah	Yard Movement		Yard Movement	
Minturn, Colo.	Salida, Colo.	1,040,241	601,793	2,416,460	1,986,402
Monarch, Colo.	Poncha Jct., Colo.	157,600	667	220,067	63,133
Montrose, Colo.	Gunnison, Colo.	17,645	12,339	42,274	37,548
Mounds, Utah	Green River, Utah	1,570,833	1,079,667	3,674,146	3,029,750
Nephi, Utah	Ephraim, Utah	16,214	14,048	35,048	35,857
Ogden, Utah	Salt Lake City, Utah	668,179	412,846	1,547,744	945,487
Ojo, Colo.	La Veta, Colo.	7,000	—	10,500	3,833
Ouray, Colo.	Montrose, Colo.	24,500	12,056	53,250	41,333
Park City, Utah	Roper, Utah	90,455	20,242	152,242	82,515
Poncha Jct., Colo.	Salida, Colo.	583,600	64,200	811,200	339,000
Provo, Utah	Springville, Utah	1,758,600	3,142,400	4,998,000	6,224,200
Pueblo, Colo.	Colorado Springs, Colo.	1,122,841	349,955	2,273,864	1,412,159
Rouse, Colo.	Rouse Jct., Colo.	80,625	375	119,250	34,375
Salida, Colo.	Pueblo, Colo.	1,499,385	554,396	3,093,469	2,164,531
Salt Lake City, Utah	Midvale, Utah	1,648,750	2,948,875	4,685,625	5,835,125
Santa Fe, N. M.	Antonito, Colo.	5,952	11,168	34,320	39,512
Silver City, Utah	Springville, Utah	186,222	18,689	278,267	110,933
Silverton, Colo.	Durango, Colo.	15,111	9,178	30,822	25,022
Soldier Summit, Utah	Colton, Utah	1,571,000	2,876,286	4,430,714	5,717,714
Somerset, Colo.	Delta, Colo.	348,930	11,163	549,233	210,884
Southern Jct., Colo.	Pueblo, Colo.	959,750	179,000	1,805,750	965,250

COURT EXHIBIT No. 2b
The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Net Ton Miles
Revenue and Company
Year Ended December 31, 1936

Roads East		Net Ton Miles		Gross Ton Miles	
		East Density	West Density	East Density	West Density
		Yard Movement		Yard Movement	
Spring Canyon Jct., Utah	Rains, Utah	1,563,267	2,793,133	4,442,733	5,532,600
Springville, Utah	Thistle, Utah	257,412	3,882	373,412	119,353
Sunnyside, Utah	Mounds, Utah	1,563,267	2,880,467	4,442,700	5,705,467
Thistle, Utah	Soldier Summit, Utah	363,375	75,667	593,313	317,292
Trinidad, Colo.	Walsenburg, Colo.	1,590,559	1,072,618	3,650,118	3,009,941
Utaline, Utah—Colo.	Grand Jct., Colo.	1,049,348	181,435	1,935,804	1,036,217
Walsenburg, Colo.	Southern Jct., Colo.	4,640	2,080	12,200	9,520
Westcliffe, Colo.	Texas Creek, Colo.				
Grand Total—Denver & Rio Grande Western R. R.		557,182	395,772	−1,276,269	1,076,357

(*) Also Garfield to Welby.
(**) Denver & Salt Lake Ry.

Rio Grande Southern R. R.			
Durango, Colo.	Ridgway, Colo.	22,614	Both Directions.

[fol. 1597] COURT EXHIBIT No. 2b

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Net Ton Miles
Revenue and Company
Year Ended December 31, 1936

Mortgage Liens	Net Ton Miles (Revenue and Company) Density	Net Ton Miles (Revenue and Company) Per Dollar of Funded Debt Outstanding Including Prior Liens
Denver & Rio Grande R.R.—1st Cons. Mtge. 4s and 4½s, 1936	659,448	.24
Rio Grande Western Ry.—1st Trust Mtge. 4s, 1939	2,458,379	.66
Rio Grande Western Ry.—1st Cons. Mtge. 4s, 1949	1,514,407	.33
Denver & Rio Grande Western R.R.—Rfdg. & Improv. Mtge. Series "A" 6s, 1974 and "B" 5s, 1978	939,898	.23*
Denver & Rio Grande Western R.R.—Gen. Mtge. 5s, 1955	939,898	.17*
Rio Grande Junction Ry.—1st Mtge. 5s, 1939	3,203,540	1.00*
Rio Grande Southern R.R.—1st Mtge. 4s, 1940	22,614	1.

* Direct and collateral lien.

Years Ended December 31	Net Ton Miles (Rev. & Co.) Density	Ratio of Revenue Ton Miles To Rev. & Company Ton Miles	Average Revenue Per Net Ton-Mile Rev. & Co. Freight (Mills)	Density Per Cent of 1936
1936	952,954	89.2%	9.3	100.0%
1935	731,907	90.8	9.7	76.8

COURT EXHIBIT No. 2c

The Denver & Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Year ended December 31, 1937

Reads East		Net Ton Miles (Revenue & Company)		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Alamo, Colo.	Walsenburg, Colo.	256,900	4[illegible]000	383,550	134,250
Alamosa, Colo.	La Veta, Colo.	299,508	209,951	805,033	681,082
Alamosa, Colo.	Mears Jct., Colo.	32,851	37,797	70,203	74,649
Antonito, Colo.	Alamosa, Colo.	153,897	71,345	332,966	242,345
Aspen, Colo.	Glenwood Springs, Colo.	28,000	7,341	74,854	53,878
Baldwin, Colo.	Gunnison, Colo.	39,333	944	58,056	19,611
Bingham, Utah	Midvale, Utah	277,000	499,419	576,968	802,645
Bon Carbo, Colo.	Trinidad, Colo.	174,294	2,765	254,176	82,118
Bond-Orestod, Colo.	Denver, Colo.	781,824	375,359	1,781,397	1,259,977
Capers, Colo.	Mustang, Colo.	12,000	—	19,500	8,000
Chama, N. M.	Antonito, Colo.	129,222	58,206	263,889	189,746
Clear Creek, Utah	Colton, Utah	40,048	2,238	61,143	25,524
Colorado Springs, Colo.	Denver, Colo.	753,849	326,425	1,582,356	1,305,740
Colton, Utah	Helper, Utah	1,774,944	2,980,500	4,861,556	5,839,167
Creede, Colo.	Alamosa, Colo.	53,072	17,362	137,884	102,971
Crested Butte, Colo.	Gunnison, Colo.	325,071	5,679	468,679	146,429
Delta, Colo.	Montrose, Colo.	74,727	137,045	253,818	264,682
Dotsero, Colo.	Bond-Orestod, Colo.	846,105	551,526	1,943,237	1,509,500
Dotsero, Colo.	Minturn, Colo.	1,149,879	1,000,190	2,703,793	2,477,414
Durango, Colo.	Chama, N. M.	78,704	45,648	166,157	131,231
Farmington, N. M.	Durango, Colo.	25,490	7,204	52,265	34,102
Glenwood Springs, Colo.	Dotsero, Colo.	1,979,935	1,524,634	4,581,071	3,932,914

Grand Jct., Colo.	Delta, Colo.	114,275	335,059	388,157	646,941
Grand Jct., Colo.	Glenwood Springs, Colo.	1,969,578	1,520,289	4,558,478	3,918,456
Green River, Utah	Utaline, Utah.-Colo.	1,708,083	1,150,319	3,940,083	3,166,042
Gunnison, Colo.	Mears Jct., Colo.	367,444	26,317	550,889	206,302
Heber, Utah	Provo, Utah	19,923	31,731	73,269	83,692
Helper, Utah	Mounds, Utah	1,702,174	1,423,913	4,069,783	3,558,826
Kenilworth Jct., Utah	Kenilworth, Utah	Yard Movement		Yard Movement	
La Veta, Colo.	Walsenburg, Colo.	342,125	292,938	905,938	816,250
Manitou, Colo.	Colorado Springs, Colo.	Yard Movement		Yard Movement	
Marysvale, Utah	Thistle, Utah	54,121	52,833	143,742	144,129
Mears Jct., Colo.	Poncha Jct., Colo.	395,833	63,500	614,167	277,833
Midvale, Utah	Provo, Utah	1,762,206	3,053,647	4,908,088	5,940,735
Midvale, Utah	Sand Pit, Utah	Yard Movement		Yard Movement	
Minturn, Colo.	Salida, Colo.	1,200,667	718,517	2,694,276	2,131,701
Monarch, Colo.	Poncha Jct., Colo.	273,533	1,533	383,533	111,200
Montrose, Colo.	Gunnison, Colo.	19,274	16,048	48,839	46,084
Mounds, Utah	Green River, Utah	1,687,250	1,136,292	3,892,042	3,127,417
Nephi, Utah	Ephraim, Utah	13,452	8,762	28,357	28,333
Ogden, Utah	Salt Lake City, Utah	721,462	458,769	1,678,897	1,106,231
Ojo, Colo.	La Veta, Colo.	4,500	667	7,000	3,667
Ouray, Colo.	Montrose, Colo.	24,278	13,944	47,306	36,472
Park City, Utah	Roper, Utah	83,970	18,758	144,697	80,636
Poncha Jct., Colo.	Salida, Colo.	688,400	67,400	1,026,800	401,400
Provo, Utah	Springville, Utah	1,943,200	3,460,800	5,412,200	6,732,800
Pueblo, Colo.	Colorado Springs, Colo.	1,109,136	392,182	2,328,091	1,568,727
Rouse, Colo.	Mayne, Colo.	87,000	2,250	127,750	41,750
Salida, Colo.	Pueblo, Colo.	1,848,823	617,760	3,613,594	2,315,656
Salt Lake City, Utah	Midvale, Utah	1,821,750	3,244,500	5,073,875	6,312,000
Santa Fe, N. M.	Antonito, Colo.	4,240	8,520	32,440	36,736
Silver City, Utah	Springville, Utah	238,178	26,422	358,733	147,622
Silverton, Colo.	Durango, Colo.	23,733	11,289	44,200	32,867
Soldier Summit, Utah	Colton, Utah	1,735,143	3,128,143	4,800,857	6,106,286
Somerset, Colo.	Delta, Colo.	328,605	19,093	507,814	198,372
Southern Jct., Colo.	Pueblo, Colo.	956,500	229,750	1,792,000	976,500

COURT EXHIBIT No. 2c—Continued

The Denver & Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees.
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Year ended December 31, 1937

Reads East		Net Ton Miles (Revenue & Company)		Gross Ton Miles	
		East Density	West Density	East Density	West Density
		Yard Movement		Yard Movement	
Spring Canyon Jct., Utah	Rains, Utah	1,727,267	3,076,267	4,810,800	5,984,733
Springville, Utah	Thistle, Utah	283,118	3,471	411,647	132,471
Sunnyside, Utah	Mounds, Utah	1,727,267	3,172,400	4,810,800	6,171,733
Thistle, Utah	Soldier Summit, Utah	439,634	82,390	704,756	349,488
Trinidad, Colo.	Walsenburg, Colo.**	1,676,235	1,128,882	3,866,618	3,107,000
Utaline, Utah-Colo.	Grand Jct., Colo.	1,079,870	254,000	1,978,087	1,088,696
Walsenburg, Colo.	Southern Jct., Colo.	4,400	1,800	11,720	8,320
Westcliffe, Colo.	Texas Creek, Colo.				
Grand Total—Denver & Rio Grande Western R. R.		602,352	438,338	1,358,878	1,146,166

* Also Garfield to Welby.
\# Over Denver & Salt Lake Ry.
** Colorado & Southern Ry. Tracks.

[fol. 1599] COURT EXHIBIT No. 2c

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density.
Year Ended December 31, 1937

Mortgage Liens	Net Ton Miles (Revenue and Company) Density	Net Ton Miles (Revenue and Company) Per Dollar of Funded Debt Outstanding Including Prior Liens
Denver & Rio Grande Western R.R.—Trustees' Certificates Series "D" due Feb. 1, 1939 and Series "E" due Feb. 2, 1939	986,591	447
Denver & Rio Grande R.R.—1st Cons. Mtge. 4s & 4½s, 1936	736,216	25
Rio Grande Western Ry.—1st Trust Mtge. 4s, 1939	2,668,066	68
Rio Grande Western Ry.—1st Cons. Mtge. 4s, 1949	1,651,819	34
Denver & Rio Grande Western R.R.—Rfdg. & Improv. Mtge. Series "A" 6s, 1974 and "B" 5s, 1978	1,053,224	24*
Denver & Rio Grande Western R.R.—Gen. Mtge. 5s, 1955	1,053,224	18*
Rio Grande Junction Ry.—1st Mtge. 5s, 1939	3,485,369	108

* Direct and collateral lien.

Years Ended December 31	Net Ton Miles (Rev. & Co.) Density	Ratio of Revenue Ton Miles To Rev. & Company Ton Miles	Average Revenue Per Net Ton Mile Rev. & Co. Freight (Mills)	Density Per Cent of 1937
1937	1,040,690	87.6%	8.9	100.0%
1936	952,954	89.2	9.3	91.6

[fol. 1600]

COURT EXHIBIT No. 2d

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Year Ended December 31, 1938

Reads East		Net Ton Miles (Revenue & Company)		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Alamo, Colo.	Walsenburg, Colo.	185,800	3,150	282,300	99,450
Alamosa, Colo.	La Veta, Colo.	241,213	170,393	634,852	564,262
Alamosa, Colo.	Mears Jct., Colo.	13,824	34,297	36,419	59,878
Antonito, Colo.	Alamosa, Colo.	136,172	55,207	289,897	205,345
Aspen, Colo.	Glenwood Springs, Colo.	23,854	9,341	68,049	54,293
Baldwin, Colo.	Gunnison, Colo.	35,444	944	51,722	17,944
Bingham, Utah	Midvale, Utah	258,452	516,677	540,516	800,355
Bon Carbo, Colo.	Trinidad, Colo.	130,529	2,235	191,647	62,353
Bond—Orestod, Colo.	Denver, Colo.	620,718	361,733	1,537,321	1,127,672
Capers, Colo.	Mustang, Colo.	2,500	—	4,500	2,000
Chama, N. M.	Antonito, Colo.	115,206	41,714	230,968	156,937
Clear Creek, Utah	Colton, Utah	63,667	2,429	98,524	37,048
Colorado Springs, Colo.	Denver, Colo.	607,753	262,836	1,306,027	1,093,795
Colton, Utah	Helper, Utah	1,392,333	2,661,500	4,135,167	5,206,611
Creede, Colo.	Alamosa, Colo.	30,333	17,420	92,246	79,797
Crested Butte, Colo.	Gunnison, Colo.	201,071	3,286	286,464	89,036
Delta, Colo.	Montrose, Colo.	64,773	126,682	242,273	249,045
Dotsero, Colo.	Bond—Orestod, Colo.	677,974	495,605	1,676,079	1,304,026
Dotsero, Colo.	Minturn, Colo.	956,793	647,328	2,329,172	1,950,534
Durango, Colo.	Chama, N. M.	73,574	31,481	147,611	107,148
Farmington, N. M.	Durango, Colo.	20,551	5,122	43,408	28,816

Glenwood Springs, Colo.	Dotsero, Colo.	1,594,571	1,476,883	3,895,672	3,287,701
Grand Jct., Colo.	Delta, Colo.	99,059	309,686	370,529	608,804
Grand Jct., Colo.	Glenwood Springs, Colo.	1,587,222	1,169,911	3,877,378	3,271,789
Green River, Utah	Utahne, Utah-Colo.	1,341,236	1,039,903	3,304,278	2,846,819
Gunnison, Colo.	Mears Jct., Colo.	230,730	19,571	352,556	139,032
Heber, Utah	Provo, Utah	17,115	32,000	67,115	81,962
Helper, Utah	Mounds, Utah	1,339,000	1,311,391	3,427,522	3,235,087
Kenilworth Jct., Utah	Kenilworth, Utah	Yard Movement		Yard Movement	
La Veta, Colo.	Walsenburg, Colo.	273,063	177,500	696,813	599,063
Manitou, Colo.	Colorado Springs, Colo.	Yard Movement		Yard Movement	
Marysvale, Utah	Thistle, Utah	55,553	51,250	145,879	140,636
Mears Jct., Colo.	Poncha Jct., Colo.	241,667	53,333	384,500	196,833
Midvale, Utah	Provo, Utah	1,371,618	2,669,441	4,166,118	5,200,853
Midvale, Utah	Sand Pit, Utah	Yard Movement		Yard Movement	
Minturn, Colo.	Salida, Colo.	882,977	452,989	2,142,885	1,699,897
Monarch, Colo.	Poncha Jct., Colo.	112,133	267	157,933	46,867
Montrose, Colo.	Gunnison, Colo.	17,516	12,306	46,161	40,226
Mounds, Utah	Green River, Utah	1,324,875	1,027,208	3,263,979	2,812,104
Nephi, Utah	Ephraim, Utah	13,238	9,405	27,667	28,738
Ogden, Utah	Salt Lake City, Utah	603,256	420,436	1,461,256	995,000
Ojo, Colo.	La Veta, Colo.	5,833	—	8,667	2,500
Ouray, Colo.	Montrose, Colo.	28,972	12,009	56,278	37,389
Park City, Utah	Roper, Utah	70,424	10,212	121,667	61,121
Poncha Jct., Colo.	Salida, Colo.	365,600	55,800	561,000	252,260
Provo, Utah	Springville, Utah	1,512,600	3,025,400	4,594,000	5,894,400
Pueblo, Colo.	Colorado Springs, Colo.	894,182	315,773	1,921,500	1,314,114
Rouse, Colo.	Mayne, Colo.	44,000	500	66,500	23,500
Salida, Colo.	Pueblo, Colo.	1,183,260	453,927	2,607,281	1,857,635
Salt Lake City, Utah	Midvale, Utah	1,418,000	2,836,250	4,306,875	5,525,875
Santa Fe, N. M.	Antonito, Colo.	2,448	9,640	25,808	32,896
Silver City, Utah	Springville, Utah	215,511	23,689	326,378	135,000
Silverton, Colo.	Durango, Colo.	35,956	8,133	59,333	31,022
Soldier Summit, Utah	Colton, Utah	1,329,143	2,792,857	4,037,286	5,429,857
Somerset, Colo.	Delta, Colo.	301,047	11,209	477,488	186,535
Southern Jct., Colo.	Pueblo, Colo.	716,000	164,250	1,342,750	765,000

COURT EXHIBIT No. 2d—Continued

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Year Ended December 31, 1938

Reads East		Net Ton Miles (Revenue & Company)		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Spring Canyon Jct., Utah	Rains, Utah	Yard Movement		Yard Movement	
Springville, Utah	Thistle, Utah	1,344,467	2,689,200	4,083,533	5,239,400
Sunnyside, Utah	Mounds, Utah	296,588	4,529	430,235	144,882
Thistle, Utah	Soldier Summit, Utah	1,344,433	2,773,233	4,083,533	5,463,133
Trinidad, Colo.	Walsenburg, Colo.**	274,341	59,366	449,439	244,049
Utaline, Utah-Colo.	Grand Jct., Colo.	1,316,235	1,020,500	3,242,647	2,793,706
Walsenburg, Colo.	Southern Jct., Colo.	762,935	160,478	1,410,457	815,326
Grand Total		464,940	368,253	1,122,843	985,433

(*) Also Garfield to Welby.
(#) Over Denver & Salt Lake Ry.
(##) Dotsero Cutoff.
(**) C. & S. Ry. Tracks.

[fol. 1601] COURT EXHIBIT No. 2d

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Year Ended December 31, 1938

	Net Ton Miles (Revenue and Company) Density	Net Ton Miles (Revenue and Company) Per Dollar of Funded Debt Outstanding Including Prior Liens
Denver & Rio Grande Western R.R.—Trustees' Certificates Series "G" 3½s, 1942	785,213	356
Denver & Rio Grande R.R.—1st Cons. Mtge. 4's, & 4½'s, 1936	546,626	18
Rio Grande Western Ry.—1st Trust Mtge. 4's, 1939	2,250,202	57
Rio Grande Western Ry.—1st Cons. Mtge. 4's, 1949	1,400,716	29
Denver & Rio Grande Western R.R.—Refdg. & Improv. Mtge. Series "A" 6's, 1974 and "B" 5's, 1978	837,705	19*
Denver & Rio Grande Western R.R.—Gen. Mtge. 5's, 1955	837,705	14*
Rio Grande Junction Ry.—1st Mtge. 5's, 1939	2,753,580	86

* Direct and Collateral Lien.

Years Ended December 31	Net Ton Miles (Rev. & Co.) Density	Ratio of Revenue Ton Miles To Rev. & Company Ton Miles	Average Revenue Per Net Ton Mile Rev. & Co. Freight (Mills)	Density Per Cent of 1938
1938	833,193	92.8%	9.7	100.0%
1937	1,040,690	87.6	8.9	124.9

[fol. 1602]

COURT EXHIBIT No. 2e

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver and Rio Grande Western Railroad
Freight Traffic Density
Year Ended December 31, 1939

Reads East		Net Ton Miles (Revenue & Company)		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Alamo, Colo.	Walsenburg, Colo.	218,750	3,750	324,250	109,650
Alamosa, Colo.	La Veta, Colo.	217,803	151,016	622,754	559,131
Alamosa, Colo.	Mears Jct., Colo.	10,216	29,986	32,054	51,973
Antonito, Colo.	Alamosa, Colo.	133,310	59,448	282,034	202,976
Aspen, Colo.	Glenwood Springs, Colo.	25,732	10,098	68,634	52,220
Baldwin, Colo.	Gunnison, Colo.	26,056	944	38,722	13,667
Bingham, Utah	Midvale, Utah	294,097	513,871	610,452	821,419
Bon Carbo, Colo.	Trinidad, Colo.	150,706	2,000	220,471	71,471
Bond-Orestod, Colo.	Denver, Colo.*	718,214	431,321	1,756,023	1,304,519
Capers, Colo.	Mustang, Colo.	8,000	—	11,500	5,500
Chama, N. M.	Antonito, Colo.	108,651	43,238	220,032	154,413
Clear Creek, Utah	Colton, Utah	49,810	3,476	75,619	29,714
Colorado Springs, Colo.	Denver, Colo.	663,479	280,411	1,403,178	1,178,151
Colton, Utah	Helper, Utah	1,667,667	2,912,111	4,663,278	5,806,889
Creede, Colo.	Alamosa, Colo.	34,841	17,420	97,406	81,246
Crested Butte, Colo.	Gunnison, Colo.	221,143	2,357	314,357	96,286
Delta, Colo.	Montrose, Colo.	60,955	131,091	228,000	246,136
Dotsero, Colo.	Bond—Orestod, Colo.**	779,263	540,184	1,900,026	1,459,868
Dotsero, Colo.	Minturn, Colo.	1,034,414	760,103	2,431,845	2,203,724
Durango, Colo.	Chama, N. M.	52,574	30,593	115,574	92,472
Farmington, N. M.	Durango, Colo.	20,653	5,122	44,020	27,959

Glenwood Springs, Colo.	Dotsero, Colo.	1,806,747	1,306,603	4,288,734	3,659,169
Grand Jct., Colo.	Delta, Colo.	93,196	320,471	348,667	601,647
Grand Jct., Colo.	Glenwood Springs, Colo.	1,796,800	1,299,789	4,264,411	3,642,511
Green River, Utah	Utaline, Utah-Colo.	1,572,611	1,198,167	3,741,681	3,265,347
Gunnison, Colo.	Mears Jct., Colo.	242,889	11,746	368,270	133,984
Heber, Utah	Provo, Utah	15,615	85,846	88,731	159,115
Helper, Utah	Mounds, Utah	1,567,696	1,503,304	3,894,826	3,693,826
Kenilworth Jct., Utah	Kenilworth, Utah	Yard Movement		Yard Movement	
La Veta, Colo.	Walsenburg, Colo.	241,458	164,688	678,563	597,750
Marysvale, Utah	Thistle, Utah	53,121	50,212	137,871	136,902
Mears Jct., Colo.	Poncha Jct., Colo.	250,767	41,333	395,666	183,833
Midvale, Utah	Provo, Utah	1,660,676	2,873,265	4,697,412	5,743,000
Midvale, Utah	Sand Pit, Utah	Yard Movement		Yard Movement	
Minturn, Colo.	Salida, Colo.	982,356	481,287	2,249,667	1,818,460
Monarch, Colo.	Poncha Jct., Colo.	233,267	2,000	331,800	96,733
Montrose, Colo.	Gunnison, Colo.	20,484	10,242	48,581	37,871
Mounds, Utah	Green River, Utah	1,553,438	1,183,563	3,696,042	3,226,021
Nephi, Utah	Ephraim, Utah	11,833	9,119	24,762	27,000
Ogden, Utah	Salt Lake City, Utah	710,385	484,128	1,658,795	1,151,000
Ouray, Colo.	Montrose, Colo.	35,389	7,111	61,806	33,333
Park City, Utah	Roper, Utah	66,182	13,000	107,788	55,697
Poncha Jct., Colo.	Salida, Colo.	495,600	44,800	746,800	288,800
Provo, Utah	Springville, Utah	1,831,200	3,256,400	5,179,800	6,508,800
Pueblo, Colo.	Colorado Springs, Colo.	976,136	336,886	2,064,455	1,415,432
Rouse, Colo.	Mayne, Colo.	69,500	500	102,000	33,000
Salida, Colo.	Pueblo, Colo.	1,452,656	471,302	2,949,094	2,038,875
Salt Lake City, Utah	Midvale, Utah	1,716,750	3,052,875	4,856,125	6,102,000
Santa Fe, N. M.	Antonito, Colo.	2,280	9,360	26,408	33,992
Silver City, Utah	Springville, Utah	258,556	21,156	383,800	147,444
Silverton, Colo.	Durango, Colo.	10,067	5,356	21,556	16,556
Soldier Summit, Utah	Colton, Utah	1,618,143	3,055,000	4,588,143	6,068,000
Somerset, Colo.	Delta, Colo.	302,907	10,116	471,047	173,488
Southern Jct., Colo.	Pueblo, Colo.	704,000	148,250	1,331,250	739,500
Spring Canyon Jct., Utah	Rains, Utah	Yard Movement		Yard Movement	
Springville, Utah	Thistle, Utah	1,627,733	2,894,533	4,604,267	5,785,533
Sunnyside, Utah	Mounds, Utah	358,000	3,118	514,941	160,706

COURT EXHIBIT No. 2e—Continued

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver and Rio Grande Western Railroad
Freight Traffic Density
Year Ended December 31, 1939

Reads East		Net Ton Miles (Revenue & Company)		Gross Ton Miles	
		East Density	West Density	East Density	West Density
Thistle, Utah	Soldiers Summit, Utah	1,627,767	2,985,000	4,604,300	5,966,367
Trinidad, Colo.	Walsenburg, Colo.**	329,293	49,415	526,829	253,024
Utaline, Utah-Colo.	Grand Jct., Colo.	1,543,265	1,175,824	3,671,882	3,204,941
Walsenburg, Colo.	Southern Jct., Colo.	787,457	146,261	1,464,457	825,022
Grand Total		532,780	404,936	1,242,663	1,092,974

(*) Also Garfield to Welby.
(#) Over Denver & Salt Lake Ry.
(##) Dotsero Cutoff.
(**) C. & S. Ry. Tracks.

[fol. 1603] COURT EXHIBIT No. 2e

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees
(Copy from H. H. Copeland & Son)

Denver & Rio Grande Western R. R.
Freight Traffic Density
Year Ended December 31, 1939

Mortgage Liens	Net Ton Miles (Revenue and Company) Density	Net Ton Miles (Revenue and Company) Per Dollar of Funded Debt Outstanding Including Prior Liens
Denver & Rio Grande Western R.R.—Trustees' Ctfs. Series "G" 3½s, 1942	881,555	397
Denver & Rio Grande R.R.—1st Cons. Mtge. 4s and 4½s, 1936	598,390	20
Rio Grande Western Ry.—1st Trust Mtge. 4s, 1939	2,563,056	65
Rio Grande Western Ry.—1st Cons. Mtge. 4s, 1949	1,593,371	33
Rio Grande Junction Ry.—1st Mtge. 5s, 1939	3,092,598	96
Denver & Rio Grande Western R.R.—Rfdg. & Improv. Mtge Series "A" 6s, 1974 and "B" 5s, 1978	940,807	21*
Denver & Rio Grande Western R.R.—Gen. Mtge. 5s, 1955	940,807	16*

* Direct and collateral lien.

Years Ended December 31	Net Ton Miles (Rev. & Co.) Density	Ratio of Revenue Ton Miles To Rev. & Company Ton Miles	Average Revenue Per Net Ton Mile Rev. & Co. Freight (Mills)	Density Per Cent of 1939
1939	937,716	91.2%	9.3	100.0%
1938	833,193	92.8	9.7	88.9

COURT EXHIBIT NO. 3, SHEET 3

Utah Fuel Company and Subsidiary Companies

Summaries of Consolidated Income, Years Ended December 31, 1933 thru 1939

	1933	1934	1935	1936	1937	1938	1939
Gross Earnings from Sale of Coal, Coke and Merchandise	$1,295,507	$1,416,869	$1,650,287	$1,902,202	$2,273,904	$2,086,051	$2,090,258
Net Earnings from Rentals, etc.	53,261	52,283	48,692	48,692	40,470	28,784	55,409
Net Income from other Sources—Interest, etc.	9,441	7,941	12,370	8,178	6,495	4,081	4,563
Total Income	$1,358,209	$1,477,093	$1,711,349	$1,959,009	$2,320,869	$2,118,316	$2,150,230
Operating Expenses	$979,383	$1,097,727	$1,303,148	$1,563,959	$1,810,535	$1,623,700	$1,632,598
Income Charges	477,880	425,492	405,210	383,988	421,888	443,450	454,458
Total Cost	$1,457,263	$1,523,219	$1,708,358	$1,947,947	$2,232,423	$2,067,150	$2,087,056
Total Net Income before Charging Federal Income Taxes	(d) $99,054	(d) $46,126	2,991	$11,062	$88,446	$51,766	$63,174
Provision for Federal Income Taxes		220	2,552	3,509	19,016	10,294	17,319
Total Net Income After Charging Federal Income Taxes	(d) $99,054	(d) $46,346	$439	$7,553	$69,430	$41,472	$45,855
Adding Depreciation and Depletion Charges (Included in Income Charges above) of	292,654	234,742	221,628	216,293	226,445	236,912	236,376
Results in New Money Earned	$193,600	$188,396	$222,067	$223,846	$295,875	$278,384	$282,231
Total Depreciation and Depletion Included in above Income Charges (Affiliated Companies are: Utah Fuel Company, The Calumet Fuel Company, Wasatch Store Company, Bamberger Coal Company, Castle Gate Coal, Coke and Fuel Company for Yards at Ogden and Brigham, Utah Fuel-Coal Company, Utah Fuel Stoker Sales Company and Utah Grazing Lands Company)	$292,654	$234,742	$221,628	$216,293	$226,445	$236,912	$236,376
Consolidated Net Cost of Additions & Betterments	$85,097	$82,935	$131,318	$203,494	$278,176	$125,402	$523,528

(d) Deficit

Current

[fol. 1605]

COURT EXHIBIT No. 3, SHEET 4

Utah Fuel Company and Subsidiary Companies

Condensed Balance Sheets—By Companies and Consolidated—At December 31, 1939

Assets	Utah Fuel Co.	The Calumet Fuel Company	Wasatch Store Company	Utah Fuel Stoker Sales Company	Bamberger Coal Company	Utah Fuel-Coal Company	Utah Grazing Lands Company	Eliminations	Total
Cash	$72,583.35	$104,370.59	$65,522.12	$3,421.74	$11,912.16	$2,087.39	$913.94		$260,811.29
Accounts Receivable:									
Railroads	81,651.27	920.21							82,571.48
All others	184,821.54	11,664.11	31,811.28	1,077.03	35,542.13	3,126.95			268,043.04
Affiliated Companies	5,474.31							$5,474.31	
Bills Receivable	7,318.09								7,318.09
Inventories—Fuel, Supplies and Merchandise	144,168.63	13,159.42	55,694.91		25,347.18	9,795.79			248,165.93
Securities Owned:									
Guaranty Fund—U. S. Bonds deposited in accordance with Colorado Workmen's Compensation Act	34,788.13	53,454.38							88,242.51
Stocks of Subsidiary Companies (Par Value)	938,500.00		8,360.00					946,860.00	
Deferred Debit Items	10,006.30	3,991.25	222.35		283.03	3.45			14,506.38
Cash Surrender Value of Insurance on Life of A. B. Apperson		7,629.00							7,629.00
Property	14,383,087.32	890,531.88	55,255.28		19,169.30	765.32	38,000.00		15,386,809.10
Total	$15,862,398.94	$1,085,720.84	$216,865.94	$4,498.77	$92,253.80	$15,778.90	$38,913.94	$952,334.31	$16,364,096.82
Liabilities									
Accounts Payable:									
Pay Rolls, Vouchers, etc.	$224,996.82	$13,949.31	$22,327.53		$4,355.05	$8.50			$265,637.21
Provision for Federal Income Taxes	16,328.24		832.05				$159.50		17,319.79
Affiliated Companies						5,374.31	100.00	$5,474.31	
Accrued Expenses	12,999.76	7,655.43	1,026.62		1,309.37	119.74	25.00		23,129.92
Reserves	2,827,689.18	367,498.62	37,129.79		6,272.22	210.55			3,238,800.36
Capital Stock	10,000,000.00	665,500.00	150,000.00	$8,360.00	75,000.00	10,000.00	38,000.00	946,860.00	10,000,000.00
Excess of Par Value over Cost of Stock of Subsidiaries	43,599.29								43,599.29
Surplus	2,736,785.65	31,117.48	5,555.95	*3,861.23	*5,317.16	65.80	629.44		2,775,610.25
Total	$15,862,398.94	$1,085,720.84	$216,865.94	$4,498.77	$92,253.80	$15,778.90	$38,913.94	$952,334.31	$16,364,096.82

Salt Lake City, Utah
July 19, 1940

* Denotes red figure.

Correct:
(Signed) R. D. Pomeroy
Auditor

[fol. 1606]

GUARANTY TRUST EXHIBIT 5

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Net Tons (Revenue and Company) per mile of road

Movement by:	D&SLW RR	D&SL Ry.		
		Joint Line		Non-Joint
	D&RGW RR	D&RGW RR	D&SL Ry	D&SL Ry
		Eastward		
1936	826,000	772,000	986,000	665,000
1937	846,000	782,000	898,000	685,000
1938	678,000	621,000	692,000	581,000
1939	779,000	718,000	725,000	576,000
		Westward		
1936	449,000	326,000	77,000	52,000
1937	552,000	375,000	60,000	47,000
1938	496,000	362,000	43,000	36,000
1939	540,000	431,000	43,000	35,000

Accounting Department,
August 6, 1940.

[fol. 1607]

EXHIBIT No. 1

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Expenditures for Additions to and Betterments
(Excludes Retirements)

	Road					
	D&RGW	Improvements on Leased Lines	Total Road	Equipment	Total Road & Equipment	Operating Expenses in Connection with Improvements
2 Months 1935	61,190	9,217	70,407	3,307	73,714	51,400
Year 1936	1,447,272	135,799	1,583,071	631,554	2,214,625	930,070
1937	2,521,147	455,116	2,976,233	1,703,544	4,679,777	1,569,985
1938	854,377	84,953	939,330	2,068,759	3,008,089	742,820
1939	984,074	130,244	1,114,318	1,986,261	3,100,579	1,272,409
1940	922,516	41,319	963,835	2,440,936	3,404,771	1,075,428
1941	1,214,151	138,182	1,352,333	4,857,383	6,209,716	1,238,561
	8,004,697	994,830	8,999,527	13,691,744	22,691,271	6,881,673
1942 (Estimated)	2,991,761	276,782	3,268,543	4,317,580	7,586,123	1,578,955
	$10,996,458	$1,271,612	$12,268,070	$18,009,324	$30,277,394	$8,460,628

NOTE: 1942 figures based on completion of all authorized work.

Accounting Department,
October 22, 1942.

[fol. 1608] EXHIBIT No. 2

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Condensed Income Account

	1941 Actual	1942 8 mos. Actual 4 mos. Estimated
Operating Revenues	$31,572,624	$53,885,005
Operating Expenses	24,219,120	30,644,991
Net Revenue	7,353,504	23,240,014
Taxes and Rents (Excluding Income Taxes)	2,836,425	3,500,000
Net Railway Operating Income	4,517,079	19,740,014
Other Income, Net	32,751 Dr.	50,000 Dr.
Available for Interest and Income Taxes	4,484,328	19,690,014
Interest	6,786,242	5,974,294
Income Taxes		1,300,000
Net Income	$2,301,914 Dr.	$12,415,720

Accounting Department,
Denver, Colo., Oct. 22, 1942.

[fol. 1609] EXHIBIT No. 3

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Cash on hand at close of business Oct. 21, 1942		$7,468,482.09
Estimated cash balance as of Dec. 31, 1942		9,557,000
Expenditures authorized or contemplated to be provided for out of cash on hand Dec. 31, 1942.		
Payment of Conditional Sales Agreements	2,282,106	
Purchase of Diesel Freight Locomotives	3,044,706	
Purchase of 1000 Freight Cars	3,582,300	
Purchase of 300 Dump Cars	990,000	
Improvement Work authorized, but not completed	3,100,000	
1942 Ad Valorem Taxes payable in 1943	470,000	
Last quarter R. R. Unemployment Taxes	175,000	
Federal and State Income Taxes	1,300,000	
		$14,944,112
Cash Working Balance Required	$1,250,000	

Accounting Department,
Denver, Colo., Oct. 22, 1942.

[fol. 1610] EXHIBIT No. 4

The Denver and Rio Grande Western Railroad Company

Wilson McCarthy and Henry Swan, Trustees

Charges to A/C 331—Equipment Depreciation for year 1942—8 mos. Actual—4 mos. Estimated	$1,387,234
Estimated charges to A/C 266—Road Property —Depreciation for year 1943	700,000

Accounting Department,
Denver, Colo., Oct. 22, 1942.

[fol. 1611] EXHIBIT No. 5

The Denver and Rio Grande Western Railroad Company

Wilson McCarthy and Henry Swan, Trustees

Estimated Income Account

The Denver and Salt Lake Railway Company

Year 1942

(8 mos. Actual—4 mos. Estimated)

Operating Revenues	$2,719,857
Operating Expenses	1,949,137
Net Operating Revenue	770,720
Taxes and Rents—Net	263,417 Cr.
Net Railway Operating Income	1,034,137
Other Net Income	12,866
Total Operating and Other Income	1,047,003
Rent of Leased Roads & Equipment, Interest on First Mortgage and Miscellaneous Income Charges	465,570
Net available for interest on Income Bonds	$581,433

Denver, Colo., Oct. 22, 1942.

[fol. 1612] EXHIBIT No. 7

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Present and Projected D&RGW Annual Equipment Disbursements Compared Depreciation Accruals

	Grand Total All Equipment	
Year	Disbursements	Amortization & Deprec.
1942	$3,687,889	$2,215,024
1943	3,661,831	3,419,965
1944	2,811,446	3,868,965
1945	2,679,455	3,868,965
1946	2,567,296	3,868,965
1947	2,560,151	3,033,941
1948	2,270,728	1,829,000
1949	2,223,021	1,380,000
1950	2,380,516	1,380,000
1951	2,234,469	1,380,000
1952	1,866,050	1,380,000
1953	1,277,814	1,380,000
1954	1,225,024	1,380,000
1955	1,177,434	1,380,000

[fol. 1613] EXHIBIT No. 8

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Average Earnings Years 1930–1941 Inclusive
Average Earnings Years 1930–1941 Inclusive

	As Recorded in Rio Grande 1941 Stockholders Report	Estimated Roadway Depreciation*	Recorded Earnings Less Roadway Depreciation
Total Operating Revenues	$23,895,598		$23,895,598
Net Railway Operating Income	2,781,862	$729,859	2,052,003
Available for Interest on Funded Debt	2,362,933	729,859	1,633,074
Net Income (After Fixed Charges)	−2,874,285**	729,859	−3,604,144**

* Annual Roadway depreciation estimated at $729,859 for Rio Grande including leased lines, but *not* including Denver & Salt Lake.

** Debit balance.

Statistical Bureau
October 22, 1942

[fol. 1614] S. L. W. EXHIBIT No. 1

Sheet 1 of 2 Sheets

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

General Balance Sheet—Asset Side
December 31, 1942

Investments:			
701 Road and Equipment Property			$225,140,315.59
702 Improvements on Leased Property			501,086.73
704 Deposits in Lieu of Mortgaged Property Sold			37,874.64
705 Miscellaneous Physical Property			221,358.20
706 Investments in Affiliated Companies—Pledged			14,472,917.38
706 Investments in Affiliated Companies—Unpledged			1,944,570.58
707 Other Investments			734.00
			$242,318,857.12
Current Assets:			
708 Cash			$10,050,149.96
709 Temporary Cash Investments			800,000.00
711 Special Deposits			840,972.34
714 Net Balance Receivable from Agents and Conductors			420,077.75
715 Miscellaneous Accounts Receivable			4,326,907.71
716 Material and Supplies			4,487,379.21
719 Other Current Assets			59,065.57
			$20,983,652.54
Deferred Assets:			
720 Working Fund Advances			$5,175.80
722 Other Deferred Assets			531,225.89
			$536,401.69
Unadjusted Debits:			
723 Rents and Insurance Premiums Paid in Advance			$35,525.36
727 Other Unadjusted Debits			4,986,233.10
			$5,021,758.46
728 Securities Issued or Assumed—Unpledged—Held by Company	$12,400.00		
729 Securities Issued or Assumed—Pledged			
(Redeemed—Held by Trustee)	$8,333,000.00		
Pledged (Held as Collateral)	13,331,000.00		
	$21,664,000.00		
	$21,676,400.00		$268,860,669.81

[fol. 1615] Sheet 2 of 2 Sheets

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

General Balance Sheet—Liability Side

December 31, 1942

Stock:		
751 Capital Stock:		
Common		$62,457,539.62
Preferred		16,433,200.00
752 Stock Liability for Conversion		12,400.00
		$78,903,139.62
Long-Term Debt:		
755 Funded Debt Unmatured		$58,888,000.00
755½ Long-Term Debt in Default		61,328,000.00
756 Trustees' Securities		5,758,000.00
757 Amounts Payable to Affiliated Companies		4,290,826.65
Total		$130,264,826.65
Total Capital Liabilities		$209,167,966.27
Governmental Grants:		
754 Grants in Aid of Construction		$1,575,754.75
Current Liabilities:		
758 Loans and Bills Payable		$3,746,847.01
759 Traffic and Car-Service Balances—Cr.		1,719,643.35
760 Audited Accounts and Wages Payable		2,912,444.57
761 Miscellaneous Accounts Payable		844,216.79
762 Interest Matured Unpaid		113,569.37
764 Unmatured Interest Accrued		996,431.24
766 Unmatured Rents Accrued		21,804.28
767 Accrued Tax Liability		3,585,816.60
768 Other Current Liabilities		231,802.29
		$14,172,575.50
Deferred Liabilities:		
769½ Matured Interest in Default		$45,286,720.18
770 Other Deferred Liabilities		295,412.48
		$45,582,132.66
Unadjusted Credits:		
772 Premium on Funded Debt		$12,209.10
775½ Accrued Amortization of Defense Projects—Road		706.92
776 Accrued Depreciation—Equipment		15,351,301.89
776½ Accrued Amortization of Defense Projects—Equipment		743,281.78
778 Other Unadjusted Credits		544,215.96
		$16,651,715.65
Corporate Surplus:		
779 Additions to Property through Income & Surplus		$387,294.25
784 Profit and Loss	(Dr)	18,676,769.27
Total Corporate Surplus	(Dr)	$18,289,475.02
		$268,860,669.81

Accounting Department,
April 12, 1943.

[fol. 1616]

S. L. W. Exhibit No. 2

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Income Account

	1942	Two Months to February 28, 1943
Operating Revenues:		
Freight	$46,950,677.01	$8,373,525.73
Passenger	5,205,085.21	1,356,634.07
Mail	392,005.64	63,536.45
Express	730,438.84	80,663.36
Miscellaneous	1,197,289.06	258,391.12
Operating Revenues	$54,475,495.76	$10,132,750.73
Operating Expenses	$31,260,694.28	$5,967,611.50
Net Revenue from Operation	$23,214,801.48	$4,165,139.23
Railway Tax Accruals	$4,985,816.16	$1,412,528.58
Railway Operating Income	$18,228,985.32	$2,752,610.65
Hire of Equipment—Receipts	1,976,299.16	380,282.32
Joint Facility Rent Income	572,989.28	97,836.91
Gross Operating Income	$20,778,273.76	$3,230,729.88
Hire of Equipment—Payments	2,651,769.89	643,646.83
Joint Facility Rents	897,298.29	157,056.54
Net Railway Operating Income	$17,229,205.58	$2,430,026.51
Other Income	200,566.84	13,936.96
Total	$17,429,772.42	$2,443,963.47
Fixed Charges:		
Rent for Leased Roads & Equipment	$111,709.45	$18,724.70
Interest on Funded Debt	5,737,454.79	943,175.36
Interest on Unfunded Debt	268,696.81	34,335.57
Amortization of Discount on Funded Debt	4,945.77	
Total Fixed Charges	$6,122,806.82	$996,235.63
Net Income	$11,306,965.60	$1,447,727.84

Accounting Department,
April 12, 1943.

S.L.W. EXHIBIT NO. 5

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY
Wilson Mc Carthy and Henry Swan, Trustees

PAYMENTS BY DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY
TO DENVER AND SALT LAKE RAILWAY COMPANY
IN CONNECTION WITH JOINT OPERATION BETWEEN L.P. 1.5 NORTHWESTERN TERMINAL MAIN LINE AN
CALENDAR YEARS 1940, 1941 AND 1942.

	Year Ending December 31, 1940				Year Ending December 31,1941				
	Recurring Charges	Extraordinary Charges	Other Non-Recurring Charges	Total	Recurring Charges	Extraordinary Charges	Other Non-Recurring Charges	Total	Recur Char
Interest Rental-Agreed contract valuation Joint Line	$300,000			$300,000	$300,000			$300,000	$300,
Interest Rental-Additions and Betterments Joint Line	44,428			44,428	51,065			51,065	51,
Rental-Moffat Tunnel	172,950			172,950	172,950			172,950	172,
Taxes on Joint Line	47,200			47,200	46,497			46,497	43,
Interest Rental-East and West Bound Main Lines Utah Junction	4,205			4,205	4,165			4,165	4,
Interest during construction-East and West Bound Main Lines-Utah Junction									
Interest Rental-Northwestern Terminal Main Line M.P. 1.50 - 3.18	5,315			5,315	5,595			5,595	5,
Rental of Right of Way 38th to 42nd Aves. Northwestern Terminal	500			500	500			500	
Rental paid by D & S.L. to C & S space for 48th Ave. Tank	10			10	10			10	
Taxes on Northwestern Terminal Main Line MP 1.50 - 3.18	3,593			3,593	3,475			3,475	3,
Adjustment Taxes- 1937, 1938, 1939						5,551		5,551	
Improvements-Moffat Tunnel (Relining)									
Improvements-Moffat Tunnel Section (other than tunnel relining)		$17,264		17,264		14,843		14,843	
Insurance-Joint Line including Moffat Tunnel					268			268	
Operating Expenses-Joint Line	69,366			69,366	88,139			88,139	115,
Ordinary Maintenance JointLine	144,729	3,442		148,171	213,575	3,354		216,929	358,
Maintenance Charges in connection with Improvement Work		35,353		35,353		29,587		29,587	
Tabernash Engine Terminal:									
Maintenance	206			206	930			930	
Operation	4,117			4,117	2,828			2,828	3,
Charges in connection with Improvement Work						676		676	
East and West Bound Main Lines-Utah Junction									
Maintenance and Operation	1,028			1,028	2,756	237		2,993	1,
Northwestern Terminal Main Line MP1.50-3.18:									
Maintenance and Operation	1,540								

EXHIBIT NO. 5

...DS WESTERN RAILROAD COMPANY
and Henry Swan, Trustees

GRANDE WESTERN RAILROAD COMPANY
LT LAKE RAILWAY COMPANY
.F. 1.5 NORTHWESTERN TERMINAL MAIN LINE AND ORESTOD
1940, 1941 AND 1942.

ng December 31,1941			Year Ending December 31, 1942		
Other			Other		
aordinary Non-Recurring Charges	Charges	Total	Recurring Charges	Extraordinary Non-Recurring Charges	Total
	$300,000	$300,000	$300,000		$300,000
	51,065	51,792			51,792
	172,950	172,950			172,950
	46,497	43,824			43,824
	4,165	4,155			4,155
	5,595	5,695			5,695
	500	500			500
	10	10			10
	3,475	3,427			3,427
551	5,551				
843	14,343		48,496		48,496
	268	268			268
	88,139	115,886			115,886
354	216,929	358,943			358,943
587	29,587		27,415		27,415
	930	123			123
	2,828	5,424			5,424
676	676				
237	2,993	1,941			1,941

	Charges	Charges	Charges				
Interest Rental-Agreed contract valuation Joint Line	$300,000		$300,000	$300,000		$300,000	$300
Interest Rental-Additions and Bettements Joint Line	44,428		44,428	51,065		51,065	5
Rental-Moffat Tunnel	172,950		172,950	172,950		172,950	17
Taxes on Joint Line	47,200		47,200	46,497		46,497	4
Interest Rental-East and West Bound Main Lines Utah Junction	4,205		4,205	4,165		4,165	
Interest during construction-East and West Bound Main Lines-Utah Junction							
Interest Rental-Northwestern Terminal Main Line M.P. 1.50 - 3.18	5,315		5,315	5,595		5,595	
Rental of Right of Way 38th to 42nd Aves. Northwestern Terminal	500		500	500		500	
Rental paid by D & S.L. to C & S space for 48th Ave. Tank	10		10	10		10	
Taxes on Northwestern Terminal Main Line MP 1.50 - 3.18	3,593		3,593	3,475		3,475	
Adjustment Taxes- 1937, 1938, 1939					5,551	5,551	
Improvements-Moffat Tunnel (Relining)							
Improvements-Moffat Tunnel Section (other than tunnel relining)		$17,264	17,264		14,843	14,843	
Insurance-Joint Line including Moffat Tunnel				268		268	
Operating Expenses-Joint Line	69,366		69,366	88,139		88,139	11
Ordinary Maintenance JointLine	144,729	3,442	148,171	213,575	3,354	216,929	35
Maintenance Charges in connection with Improvement Work		35,353	35,353		29,587	29,587	
Tabernash Engine Terminal:							
Maintenance	206		206	930		930	
Operation	4,117		4,117	2,828		2,828	
Charges in connection with Improvement Work					676	676	
East and West Bound Main Lines-Utah Junction							
Maintenance and Operation	1,028		1,028	2,756	237	2,993	
Northwestern Terminal Main Line MP1.50-3.18:							
Maintenance and Operation	1,540		1,540	2,097		2,097	
Maintenance Charges in connection with improvement work					3,520	3,520	
Coal for D & R.G.W. Locomotives	9,698		9,698	24,341		24,341	
Miscellaneous							
Advance Surveys							
Stationery, Timetables, etc	208		208	565		565	
Wrecking Expense	2,049		2,049	10,983		10,983	
Pilot Service	222		222	2,210		2,210	
Helper Service	403		403	250		250	
Rental of Engines				4,630		4,630	
Rent of Joint Property-Credit	219		219	290		290	
Total	$811,548	$56,059	$867,607	$937,539	$57,768	$995,307	$1,1

Accounting Department
March 19, 1943

	$300,000	$300,000		$300,000
	51,065	51,792		51,792
	172,950	172,950		172,950
	46,497	43,824		43,824
	4,165	4,165		4,165
	5,595	5,695		5,695
	500	500		500
	10	10		10
	3,475	3,427		3,427
551	5,551			
843	14,843		48,496	48,496
	268	268		268
	88,139	115,866		115,866
654	216,929	358,943		358,943
587	29,587		27,415	27,415
	930	123		123
	2,828	5,424		5,424
676	676			
237	2,993	1,941		1,941
	2,097	2,326		2,326
520	3,520			
	24,341	66,377		66,377
	565	427		427
	10,983	28,871		28,871
	2,210	7,577		7,577
	250	3,136		3,136
	4,630	45,977		45,977
	290	240		240
768	$995,307	$1,219,389	$75,911	$1,295,300

S. L. W. Exhibit No. 7—Continued

547	Interest on Unfunded Debt		426.25	
551	Miscellaneous Income Charges		7,885.75	
	Total Deductions from Gross Income			1,181,889.12
	Net Income Balance Transferred to Profit and Loss			$83,909.68
	Profit and Loss			
Credits:				
602	Credit balance transferred from Income	$83,909.68		
607	Miscellaneous Credits	3,774.10		
			$87,683.78	
Debits:				
611	Debit balance, December 31, 1942	$698,302.36		
619	Loss on Retired Road and Equipment	26,452.87		
621	Miscellaneous Debits	387.80		
			725,143.03	
	Debit Balance December 31, 1942 carried to page 3			637,459.25

S. L. W. Exhibit No. 7—Continued

[fol. 1619]

Asset Side

Investments:			
701 Investment in Road and Equipment:			
Road	$15,438,564.52		
Equipment	2,274,507.59		
702 Improvements on Leased Property		$17,713,072.11	
706 Investments in Affiliated Companies:		552,109.09	
Railway Express Agency, Inc.	$19,827.93		
Ry. Expr. Agency, Inc. Capital Stock	100.00		
Railroad Credit Corporation	5,661.11	25,589.04	
Current Assets:			$18,290,770.24
708 Cash			
Agents & Condrs. Remittances in transit	$657,220.86		
	1,614.64		
711 Cash Deposited to pay coupons		$658,835.50	
Cash Deposited to pay Employees War Bond Fund		43,395.25	
713 Traffic and Car Service Balances Receivable		4,831.75	
714 Net Balance Receivable from Agents and Conductors		166,669.56	
715 Miscellaneous Accounts Receivable:		16,249.67	
U. S. Govt. Transportation Requests	$4.95		
Individuals and Companies	170,317.69		
Postmaster General	6,120.38		
Railway Express Agency, Inc.	1,895.00		
716 Material and Supplies:		178,338.02	
Stationery Stock	$5,157.70		
Roadway Stock	232,378.76		
Store Stock	218,230.42		
Fuel Stock	6,900.90		
717 Accrued Int. Receivable Ry. Expr. Agency Advances		462,667.78	
719 Other Current Assets		80.44	
		4,554.39	
			1,535,622.36

S. L. W. EXHIBIT No. 7—Continued

Deferred Assets:			
720 Working Fund Advances		$232.22	
722 Other Deferred Assets		127.94	
			360.16
Unadjusted Debits:			
723 Rents and Insurance Premiums Paid in Advance		$3,273.21	
727 Other Unadjusted Debits		101,761.90	105,035.11
728 Securities Issued or Assumed, Unpledged:			
D&SL Ry 1st Mtg. 4% Bonds	$1,000,000.00		
Total			$19,931,787.87

S. L. W. Exhibit No. 7—Continued

Unadjusted Credits:		
775 Accrued Depreciation—Road	$7,138.79	
776 Accrued Depreciation—Equipment	1,253,501.22	
778 Other Unadjusted Credits	65,894.95	1,326,534.96
Total		$20,498,791.07
Corporate Surplus:		
779 Additions to Property thru Income and Surplus	$70,456.05	
784 Profit and Loss Balance (from page 1)	*637,459.25	*567,003.20
Total		$19,931,787.87

*Red in Copy.

Denver, Colorado, February 25, 1943.

L. L. Prater,
Auditor.

[fol. 1621]

(Clerk's Note: Mr. Swan has informed this office that the exhibit he testified from on November 15, 1944, was the wrong statement and he filed a corrected statement which is here set forth.)

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Statement of Charges Under Reorganization Plan After Adjustment Account Purchase of Rio Grande Junction Bonds

			1943		1944	1945
1st Mortgage—Fixed 3%			$937,493	(Does not include pledged securities)	$937,493	$937,493
Prior Contingent 1%			312,498	(Does not include pledged securities)	312,498	312,498
Sinking Fund 1st			171,703	(Includes pledged securities)	171,703	171,703
Chase Nat'l Bank Claim (2,158,458)						
(1,524,076 1st Mtge. Bonds)	Fixed 3%	$45,722				
do	Prior Contingent 1%	15,241				
(972,998 Income Bonds)	4½%	43,785				
(1,894,332 Preferred Stock)	5%	94,717				
			$199,465*		(	
Excess of 4% on $2,158,458			113,127*		(86,338	86,338
Reconstruction Finance Corporation Claim						
(1,566,846 1st Mtge. Bonds)	Fixed 3%	$47,005				
do	Prior Contingent 1%	15,668				
(1,388,150 Income Bonds)	4½%	62,467				
(3,181,757 Preferred Stock)	5%	159,088				
			284,228†		(	
Balance on claim			271,796†		(556,024	556,024
Income Bonds 4½%			918,682	(Does not include pledged securities)	918,682	918,682
Sinking Fund Incomes			56,941	(Includes pledged securities)	56,941	56,941
5% Preferred Stock			1,606,006	(Does not include pledged securities)	1,606,006	1,606,006
Equipment Obligations						
Principal						609,000
Interest						110,284
			$4,645,685		$4,645,685	$5,364,969
Less payment under Court Order 534			2,398,679			
			$2,247,006			
1944			4,645,685			
			$6,892,691			
1945			5,364,969			
			$12,257,660			

* Excess of $86,338 constitutes a payment of principal.
† Figured on basis of collateral—Interest on claim amounts to $556,024.

Denver, Colorado,
December 28, 1944

[fol. 1618]

S. L. W. Exhibit No. 7

The Denver and Salt Lake Railway Company

Income, Profit and Loss, and General Balance Sheet
December 31, 1942

Income

Operating Income:			
501 Railway Operating Revenue		$2,880,758.56	
531 Railway Operating Expenses		1,959,407.03	
Net Revenue from Railway Operations			$921,351.53
532 Railway Tax Accruals			338,308.16
Total Operating Income			$583,043.37
Non-Operating Income:			
504 Rent from Locomotives		$59,372.97	
507 Rent from Work Equipment		2,148.94	
508 Joint Facility Rent Income		608,020.22	
509 Income from Lease of Road and Equipment		3,270.00	
510 Miscellaneous Rent Income		8,515.11	
514 Income from Funded Securities		911.43	
519 Miscellaneous Income		516.76	
Total Non-Operating Income			682,755.43
Gross Income			$1,265,798.80
Deductions from Gross Income:			
536 Hire of Freight Cars—Debit Balance		$52,817.49	
538 Rent for Passenger Train Cars		421.17	
542 Rent for Leased Roads and Equipment		394,223.27	
543 Miscellaneous Rents		6,115.19	
546 Interest on Funded Debt:			
First Mortgage Bonds		60,000.00	
Income Mortgage Bonds		660,000.00	

[fol. 1626]

Liability Side

Stock:			
751 D&SL Ry Co. Capital Stock			$5,317,104 25
Governmental Grants:			
754 Grants in Aid of Construction			105,092 88
Long Term Debt:			
755 Funded Debt Unmatured:			
D&SL Ry Co. 1st Mtg. 4% Bonds Series A	$1,500,000 00		
D&SL Ry Co. Income Mtg. 6% Gold Bonds	11,000,000 00		
D&SL Ry Co. 1st Mtg. 4% Bonds Held in Treasury	$1,000,000 00		12,500,000 00
760 Audited Accounts and Wages Payable:			
Vouchers	$112,104 34		
Pay Checks	104,762 62		
Unclaimed Wages	325 97		
Discharge Checks	1,097 28		
761 Miscellaneous Accounts Payable:		$218,290 21	
Colorado State Service Tax	10		
Colorado State Sales Tax	3 88		
Passenger Refund Drafts	63 01		
Agents Advance Charge Drafts	3,151 07		
762 Interest Matured Unpaid:		3,218 06	
Bond Coupons D&SLRy 1st Mtg 4% Bonds	$29,160 00		
Bond Coupons D&SLRy 1st Mtg 6% Bonds	60 00		
Bond Coupons D&SLRy Income Mtg. Bonds	14,175 25		
764 Unmatured Interest Accrued:		43,395 25	
Accrued Int. D&SLRy 6% Income Mortage Bonds		660,000 00	
767 Accrued Tax Liability:			
Accrued Taxes		281,383 03	
768 Other Current Liabilities		37,262 32	
Deferred Liabilities:			1,243,548 87
770 Other Deferred Liabilities			6,510 11

[fol. 1622]

The Denver and Rio Grande Western Railroad Company
Wilson McCarthy and Henry Swan, Trustees

Statement of Charges Under Reorganization Plan After Adjustment Account Purchase of Rio Grande Junction Bonds

	1943	1944	1945
1st Mortgage—Fixed 3%	$937,493	$937,493	$937,493
Prior Contingent—1%	312,498	312,498	312,498
Sinking Fund 1st	171,703	171,703	171,703
Chase National Bank	86,338	86,338	86,338
Reconstruction Finance Corporation	556,024	556,024	556,024
Income Bonds—4½%	918,682	918,682	918,682
Sinking Fund—Income Bonds	56,941	56,941	56,941
5% Preferred Stock	1,606,006	1,606,006	1,606,006
Equipment Obligations			
Principal			609,000
Interest			110,284
	$4,645,685	$4,645,685	$5,364,969
Less payment under Court Order 534	2,398,679		
	$2,247,006		
1944	4,645,685		
	$6,892,691		
1945	5,364,969		
	$12,257,660		
Estimated Balance—1/1/1945	$5,487,000		
Government Securities	13,500,000		
Tax Notes	3,005,000		
Cash in Deferred Maintenance Fund	304,000		
			$22,296,000
Appropriations and Commitments,			
Reserved for Deferred Maintenance	$3,304,000		
Improvement Program & Carryover	7,000,000		
Income Tax 1944—			
Payable 1945	5,000,000		
			$15,304,000
Balance available for charges			$6,992,000
Amount required under Plan thru 1944			$6,892,691
Balance, without any consideration of 1945 earnings			$99,309

Denver, Colorado,
December 28, 1944.

[fol. 1624] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1945

No. 278

ORDER ALLOWING CERTIORARI—Filed October 8, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Jackson and Mr. Justice Burton took no part in the consideration or decision of this application.

[fol. 1625] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1945

No. 279

ORDER ALLOWING CERTIORARI—Filed October 8, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Jackson and Mr. Justice Burton took no part in the consideration or decision of this application.

[fol. 1626] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1945

No. 280

ORDER ALLOWING CERTIORARI—Filed October 8, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Jackson and Mr. Justice Burton took no part in the consideration or decision of this application.

[fol. 1627] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1945

No. 281

ORDER ALLOWING CERTIORARI—Filed October 8, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Jackson and Mr. Justice Burton took no part in the consideration or decision of this application.

[fol. 1628] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1945

No. 282

ORDER ALLOWING CERTIORARI—Filed October 8, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Jackson and Mr. Justice Burton took no part in the consideration or decision of this application.

IN THE

Supreme Court of the United States

October Term, 1945

No.'s 278-282

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

SAME *vs.* THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY, ET ALS.,

SAME *vs.* CITY BANK FARMERS TRUST COMPANY, TRUSTEE, ET ALS.,

SAME *vs.* THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

SAME *vs.* GUY A. THOMPSON, TRUSTEE, ET ALS.,

Respondents.

Supplemental Stipulation as to Printing of Record

Supplemental Stipulation as to Printing of Record

Under date of July 16, 1945 there was executed by counsel for all parties to these cases a "Stipulation as to Printing of Record for Petition for Certiorari" (herein called the Original Stipulation). By paragraph 4 of the Original Stipulation, it was stipulated that, if the Petition of the undersigned Interests of Group 1 for writs of certiorari herein should be granted, which has now been done by orders of the Supreme Court dated October 8, 1945, the printed record for further proceedings in these cases should consist of the printed record designated in the Original Stipulation for the purposes of said Petition and heretofore filed together with such additional portions of the entire record herein certified by the Circuit Court of Appeals for the Tenth Circuit to the Clerk of the Supreme Court as the respective Interests of Groups 1 and 2 should designate for that purpose, the other parties to the Original Stipulation (referred to therein as Interests of Groups 3 and 4) retaining no right to participate in such designation. The undersigned Interests of Group 1 (including all the parties so styled in the Original Stipulation) and the undersigned Interests of Group 2 (including all the parties so styled in the Original Stipulation) desire to agree on such designation of additional portions of the record to be printed.

NOW, THEREFORE, except as may be otherwise directed by the Supreme Court, the undersigned hereby stipulate and agree that:

1. The additional portions of the record to be printed in order to constitute, with the printed record heretofore filed herein, the printed record on which these cases shall be heard, shall be the following:

(a) Those opinions, orders and documents (or portions thereof) referred to in Exhibit A hereto;

(b) Those excerpts from the testimony designated in Exhibit B hereto; and

(c) Those exhibits (or portions thereof) designated in Exhibit C hereto.

Page references in Exhibits A, B and C hereto to the transcript of the Circuit Court that are prefixed by I, or that are not prefixed by any Roman numeral, refer to pages of the transcript filed in the Circuit Court in the Approval Appeals as defined in the Original Stipulation (No.'s 2906-7 below). References to the transcript of the Circuit Court that are prefixed by II refer to pages of the transcript filed in the Circuit Court in the Confirmation Appeals as defined in the Original Stipulation (No.'s 3106-8 below). References to the transcript of the Circuit Court that are prefixed by III refer to pages of the volume certified to the Clerk of the Supreme Court by the Clerk of the Circuit Court containing the proceedings in the Circuit Court and the documents filed before it pursuant to stipulation. Page references to the transcript of hearings before the Interstate Commerce Commission or the District Court are inserted only for the convenience of the undersigned and may be disregarded by the Clerk of the Supreme Court. The documents listed in Exhibit A hereto that are prefixed by an asterisk are listed therein only for convenience and are included in the printed record already made pursuant to the Original Stipulation. The exhibits listed in Exhibit C hereto that are prefixed by an asterisk are listed therein only for clarity, are already available in printed form and, if presented to the clerk pursuant to 2. below, are not to be reprinted.

2. Any of the undersigned may present to the Clerk of the Supreme Court, for use by it as part of the printed

record aforesaid, without reprinting, thirty copies of the presently available printed forms of the following:

(a) This Stipulation (referred to in Exhibit A hereto); and

(b) The following exhibits (referred to in Exhibit C hereto);

(*i*) the Annual Reports to Stockholders of The Denver and Rio Grande Western Railroad Company (or its Debtor Trustees) for the years 1935-1943, both inclusive;

(*ii*) the Annual Reports to Stockholders of The Denver and Salt Lake Railway Company for the years 1936-1943, both inclusive; and

(*iii*) the "Income Account, Statement of Revenues and Expenses, Etc." dated January 25, 1945 and the "Income Account and Financial Exhibit" dated February 3, 1945 of The Denver and Rio Grande Western Railroad Company (by its Debtor Trustees).

The instrument referred to in (a) next above shall be bound as a part of the printed record aforesaid, but the exhibits referred to in (b) next above shall not be.

3. The affected securities owned by the member institutions of Insurance Group Committee, as shown by the record (less later sales), are:

(a) $4,501,000 principal amount of Rio Grande Western Railroad Company First Trust Mortgage Bonds (4%, due 1939);

(b) $4,500,000 principal amount of Rio Grande Western Railroad Company Consolidated Mortgage Bonds (4%, due 1949); and

(c) $2,325,000 principal amount of Denver and Rio Grande Railroad Company Consolidated Mortgage Bonds (4% and 4½%, due 1936).

4. Any of the undersigned may include in his brief a copy of the map entitled "Denver & Rio Grande Western Railroad" that was filed as Appendix A to the October 13, 1944 brief of the undersigned Interests of Group 1 in the Circuit Court, or of any later edition of said map furnished by the Debtor Trustees.

5. All the undersigned reserve the right to refer to any portion of the record certified from the Circuit Court to the Clerk of the Supreme Court (unless the Supreme Court shall require printing thereof), with the same force and effect as if such part were printed and included in the printed record herein. If it should become necessary, additional portions of said record may be designated to be printed by any of the undersigned and, upon being printed, such additional portions shall constitute a part of the printed record herein.

6. This stipulation may be executed in any number of counterparts, all of which together shall constitute but one instrument. The signatures hereto need not be on the same counterpart, but each signature, or any numbers of signatures, may be on different counterparts, or may be on separate signature sheets to be annexed to the text hereof.

Dated as of November 26, 1945.

Interests of Group 1

Signatures of Counsel	Addresses
J. Howard McGrath J. HOWARD McGRATH *Solicitor General of the United States* and	Washington, D. C.
W. Meade Fletcher, Jr. W. MEADE FLETCHER, JR. *Chief Railroad Counsel, Reconstruction Finance Corporation* *For Reconstruction Finance Corporation*	811 Vermont Ave., N. W. Washington 25, D. C.
Henry W. Anderson **By G. D. G.** HENRY W. ANDERSON and	Electric Building Richmond 12, Va.
George D. Gibson GEORGE D. GIBSON *For Insurance Group Committee*	Electric Building Richmond 12, Va.
Edwin S. S. Sunderland EDWIN S. S. SUNDERLAND and	15 Broad Street New York 5, N. Y.
James L. Homire JAMES L. HOMIRE *For Guaranty Trust Company of New York, Trustee*	15 Broad Street New York 5, N. Y.

Alexander M. Lewis	70 Broadway New York 4, N. Y.

ALEXANDER M. LEWIS
For Central Hanover Bank and Trust Company, Trustee

W. A. W. Stewart	45 Wall Street New York 5, N. Y.

W. A. W. STEWART
For United States Trust Company of New York, Trustee

Arthur A. Gammell	15 Broad Street New York 5, N. Y.

ARTHUR A. GAMMELL
For The Chase National Bank of the City of New York, Trustee

Interests of Group 2

William V. Hodges	Equitable Building Denver 2, Colorado

WILLIAM V. HODGES

and

F. C. Nicodemus	40 Wall Street New York 5, N. Y.

F. C. NICODEMUS
For (i) The Denver and Rio Grande Western Railroad Company; and
(ii) The Denver and Salt Lake Western Railroad Company

Edward E. Watts, Jr. EDWARD E. WATTS, JR.	20 Exchange Place New York 5, N. Y.

and

Milton J. Keegan MILTON J. KEEGAN *For City Bank Farmers Trust Company, Trustee*	First National Bank Bldg. Denver 2, Colorado

H. H. Larimore H. H. LARIMORE *For Guy A. Thompson, Trustee of Missouri Pacific Railroad Company*	Missouri Pacific Bldg. St. Louis 3, Missouri

EXHIBIT A

DESIGNATION OF OPINIONS, ORDERS, PLEADINGS, ETC., FOR PRINTING

Reference	Subject Matter	Printed D. Ct. Record Vol. and Pages	Beginning at C.C.A. Transcript Page
Petition of Debtor verified October 30, 1935	Filing under Section 77	1:1	I:1
Debtor's balance sheet October 1, 1935		1:559	I 439
Petition for Intervention by City Bank Farmers Trust Company, Trustee, dated Nov. 19, 1935			I 80
Answer of City Bank Farmers Trust Company, Trustee, to Petition of Trustees to borrow money dated July 13, 1936			I 637
Debtor's original Plan of Reorganization of July 28, 1936—filed July 29, 1936		2:1707–43 including Ex. B but excluding Ex. A	I 682

First plan of Insurance Group Committee—filed June 15, 1937		3:2885–2943 including plan summary	I 914
I. C. C. Examiner Jamison's Plan—filed August 12, 1938		4:4120–97 including plan summary p. 4187	II 43
*I. C. C. first Plan of July 11, 1939—filed July 31, 1939	[a cross reference to Supreme Court Transcript of Record already printed p. 29, including plan summary p. 352]		
*I C. C. Modified Plan of April 2, 1940	[a cross reference to Supreme Court Transcript of Record already printed pages 98 *et seq.*]		
District Court Opinion of December 6, 1940	Opinion concerning Commission's 1940 Plan	7:7124–57	I 1436
Discussion Plan of October 28, 1940—filed January 6, 1941		7:7352–70 including plan summary p. 7361	II 122
District Court's Plan in Opinion of March 6, 1941		7:7684–99 including Ex. A opposite p. 7698	I 1516

EXHIBIT A—CONTINUED

Reference	Subject Matter	Printed D. Ct. Record Vol. and Pages	Beginning at C.C.A. Transcript Page
I. C. C. Examiner Jamison's Plan of August 26, 1941—filed September 2, 1941		8:8147–93 including App. A, facing p. 8192	I 1540
Insurance Group Plan filed October 8, 1941—Summary of Plan			II 142
*I. C. C. Plan of July 13, 1942—filed July 27, 1942	[a cross reference to Supreme Court Transcript of Record already printed pages 113 *et seq.* and plan summary pages 353-5]		
*I. C. C. Plan of June 14, 1943—filed June 28, 1943	[a cross reference to Supreme Court Transcript of Record already printed pages 151 *et seq.* and plan summary pages 182-6]		
Debtor's balance sheet at May 31, 1943 and income statement for May, 1943		9:10,211	I 1786
Petition of City Bank Farmers Trust Co. to Commission dated August 20, 1942			II 143

10

Debtor's Petition for further hearing dated April 30, 1943		I 1816
Commission's Order denying Debtor's Petition for reopening of proceeding		I 1784
Commission's Order denying Debtor's Petition for further hearing		I 1831
Debtor's Objections to the Plan		I 1812
Joint Statement by Debtor and Subsidiary Debtor of Points to be relied on upon appeal	Appeal from Order approving Plan	I 1912
D. Ct. Order No. 478	Affirming SLW lease and SL trackage agreement	I 1824
D. Ct. Order No. 534	Authorizing first payment of interest	II 153
Petition of City Bank Farmers Trust Company dated March 28, 1944 (excluding memorandum on pp. 6-14)	For reallocation of securities	II 148
Answer by Insurance Group Committee, *et als.*		II 185

EXHIBIT A—CONTINUED

Reference	Subject Matter	Printed D. Ct. Record Vol. and Pages	Beginning at C.C.A. Transcript Page
Objections of City Bank Farmers Trust Co. to Plan			II 177
Notice of appeal by City Bank Farmers Trust Company			II 489
Statement of Points on which City Bank Farmers Trust Company intends to rely			II 493
Objections of Guy A. Thompson, Trustee, to Plan			II 172
Orders of the Supreme Court dated October 8, 1945, granting writs of certiorari			
*The Supplemental Stipulation to which this Exhibit is annexed (and attached exhibits)	Designating record for printing in the Supreme Court		

EXHIBIT B

DESIGNATION OF TESTIMONY FOR PRINTING

Beginning at					Ending at				
C.C.A. Tr.		I.C.C. Tr.		With the Word(s)	C.C.A. Tr.		I.C.C. Tr.		After the Word(s)
Page	Line	Page	Line		Page	Line	Page	Line	
Transcript of Hearings before Interstate Commerce Commission									
1957	1	1	1	Before	1960	8	4	8	1924
1967	11	12	11	Since	1969	10	14	10	satisfactory.
1972	13	20	13	William	1972	21	20	21	reorganization.
1976	13	38	13	Q	1984	16	46	16	evidence.)
1996	15	66	15	When	1999	1	69	1	well.
2002	14	72	14	It	2003	21	73	21	work.
2006	6	79	6	Q	2056	5	129	5	evidence.)
2081	1	158	1	Mr.	2081	26	159	1	evidence.)
2082	2	167	2	The	2104	12	189	12	evidence.)
2105	22	191	22	Q	2108	22	194	22	cash.
2109	17	195	17	Mr.	2110	21	196	21	identification.)
2111	15	197	15	The	2114	13	200	13	later.
2117	8	204	8	Now	2128	25	214	25	evidence.)
2129	4	216	4	Q	2133	22	220	22	them.

EXHIBIT B—CONTINUED

Beginning at					Ending at				
C.C.A. Tr.		I.C.C. Tr.		With the Word(s)	C.C.A. Tr.		I.C.C. Tr.		After the Word(s)
Page	Line	Page	Line		Page	Line	Page	Line	
Transcript of Hearings before Interstate Commerce Commission—Continued									
2134	5	224	5	Q	2136	11	226	11	Corporation.
2137	20	234	20	Q	2141	12	238	12	time.
2142	4	240	4	Q	2145	10	243	10	claims.
2146	3	253	3	Q	2147	1	254	1	evidence.)
2148	24	258	24	Have	2151	19	261	19	Company.
2161	17	329	17	Therefore	2162	20	330	20	plan.
2167	10	431	10	(Exhibit	2167	10	431	10	evidence.)
2171	1	504	1	Q.	2174	24	507	24	evidence.)
2175	9	516	9	J. S. Pyeatt	2179	11	520	11	condition.
II 39	22	548	22	Q	II 40	14	549	14	Very.
2237	2	603	2	Examiner	2239	13	605	13	Stewart.
2297	23	818	23	Mr.	2319	6	840	6	obvious.
2320	1	841	1	Leonard	2364	20	855	20	evidence.
2363	2	901	2	Q	2366	4	904	4	Betterments.

2381	10	1129	10	Q
2391	18	1245	18	Q
2394	1	1258	1	Q
2397	19	1279	19	Q
2402	9	1329	9	J. S. Pyeatt
2406	9	1346	9	Q
2409	23	1350	23	Q.
2414	11	1356	11	Q.
2417	14	1393	14	T. A. Hamilton
2445	7	1463	7	T. A. Hamilton
2497	7	1649	7	(Exhibit
2497	18	1649	18	(Exhibit
2500	5	1703	5	Examiner
2504	3	1820	3	Mr.
2508	16	1848	16	Q
2520	21	1971	21	E. H. Burdick
2566	8	2066	8	Q
2575	16	2090	16	Mr.
2648	2	2163	2	Mr.
2649	1	2164	1	Frank
2674	8	2189	8	Mr.
4734	7	2214	7	Q
4762	6	2242	6	Is
4782	1	2262	1	Q
4806	5	2286	5	A
4833	6	2313	6	Mr. Marsh
4848	8	2328	8	I
4891	4	2371	4	Q

2385	24	1133	24	company.
2392	15	1246	15	it.
2394	8	1258	8	stock.
2399	16	1281	16	sir.
2405	25	1332	25	$175,000
2407	5	1347	5	so.
2413	4	1355	4	application.
2416	6	1358	6	draft.
2428	12	1404	12	exhibits.
2459	11	1474	11	is.
2497	8	1649	8	evidence.)
2497	19	1649	19	evidence.)
2500	15	1703	15	Commission.
2507	29	1824	1	witnesses.
2519	6	1859	6	2.94.
2565	6	2016	6	evidence.)
2566	19	2066	19	Yes.
2580	1	2095	1	record.
2648	16	2163	16	excused.
2658	4	2173	4	all.
2681	10	2196	10	noted
4753	17	2233	17	and 263.
4762	17	2242	17	traffic.
4802	5	2282	5	sir.
4832	20	2312	20	so.
4834	25	2314	25	objection.
4863	25	2343	25	Nothing.
4891	25	2371	25	record.

EXHIBIT B—CONTINUED

Beginning at					Ending at				
C.C.A. Tr.		D. Ct. Tr.		With the Word(s)	C.C.A. Tr.		D. Ct. Tr.		After the Word(s)
Page	Line	Page	Line		Page	Line	Page	Line	
Transcript of Hearing before District Court in July-August, 1940; on Old Plan									
4284	1	1	1	In	4286	9	2	32	Company.
4286	14	17	16	C. M. Lightburn	4362	through first paragraph	97	19	lands.
4390	10	225	6	My	4397	25	232	27	opening.
4406	27	541	18	Mr.	4407	1	541	21	admitted.
4407	15	577	23	Mr.	4408	7	578	12	No. 26.
4417	25	615	18	Q	4429	5	628	11	safely.
4441	15	648	1	Thereupon	4444	27	651	15	2-E
4445	1	653	1	Mr.	4445	4	653	4	admitted.
4454	2	869	3	Mr.	4455	8	870	10	admitted
4455	9	919	11	By	4456	29	921	2	record.)
4463	16	946	20	Q	4464	1	947	6	country.
4487	last	1278	26	Mr.	4496	last	1288	28	time.
4503	21	1302	17	Arthur Ridgway	4508	last	1308	last	excused.)

4925	2	1	1	In	4926	16	2	16	corporation.
4927	15	22	14	Q	4932	3	27	2	not.
4937	8	32	8	Q	4953	11	48	4	sir.
4959	2	57	27	Q	4960	1	58	25	Lake.
4965	2	63	26	A	4987	3	85	21	new account.
4990	16	91	5	Now	4992	3	92	21	1944.
4993	19	148	19	Mr.	5008	12	162	12	denied.

Transcript of Hearing before District Court in April, 1943, on Rental

5020	2	1	1	In	5022	13	3	10	Group.
5023	1	30	1	Henry Swan	5023	12	30	12	them.
5024	17	37	17	T. A. Thompson	5033	18	47	18	dollars.
5035	21	50	21	By	5035	27	50	27	right.
5036	8	51	8	L. L. Prater	5040	29	55	29	you.
5042	18	104	28	Mr. Gibson	5043	17	105	26	objection.
5044	1	277	7	The Court	5047	20	280	23	done.
5047	21	282	17	Mr. Gibson	5048	last	283	16	ordered.

EXHIBIT B—CONTINUED

Beginning at					Ending at				
C.C.A. Tr.		D. Ct. Tr.		With the Word(s)	C.C.A. Tr.		D. Ct. Tr.		After the Word(s)
Page	Line	Page	Line		Page	Line	Page	Line	
Transcript of Hearing before District Court in September, 1943, on Approval of Plan									
5276	2	1	1	In	5278	12	3	10	York.
5296	5	261	8	Excerpts	5304	15	270	3	Fuel.
5312	1	279	15	The Court	5315	last	283	last	taken.
Transcript of Hearing before District Court on November 15, 1944, on Improvements									
II 451	1	1	1	In	II 456	last	6	last	signed.

Transcript of Hearing before District Court on November 20, 1944

II 461	1	1	1	In	II 461	last	2	last	determine.

Transcript of Hearing before District Court on November 29, 1944

II 462	1	1	1	In	II 468	last	7	last	record ——

EXHIBIT C

DESIGNATION OF EXHIBITS FOR PRINTING

Number	Subject Matter	Beginning at C.C.A. Tr. p.
	Exhibits from Hearings before Interstate Commerce Commission	
25-25A	Consolidated balance sheet Dec. 31, 1935	2837, 2838
27	"Capitalizable Assets December 31, 1935"	2915
28	Summary of securities	2918
34 (only subdivision IV of Article Third)	Additional issue clause—Western Consol. Mortgage	474
34-J	Utah Fuel Supplement to Western Consolidated Mortgage	3099
35	Utah Fuel Agreement of Dec. 20, 1924	3171
36	Description of Utah Fuel Company (including Ex.'s A and B)	3192
37-A	1924 Supplement to R & I Mortgage	3199
69 (only the 2 paragraphs on p. 12 under caption "Utah Fuel Stock")	Text of segregation formula before revision	3675
117-117A	Normal year estimate, RG	3750, 3751
118 Facing page, Table of Contents and p. 1	" " " "	3752
119 (first table only)	" " " SL	3920
120	" " " Consolidated	3930

155	Utah Fuel Company balance sheets	3969
*209	RG annual report for 1936	4096
*210	SL " " " "	4134
246	RG books less depreciation	4168
253 (only C.C.A. Tr. pages 4169-70, 4173-83, 4189, 4191, 4195-6, 4198-9 and 4203)	Utah Fuel study	4169
*260	RG annual report for 1940	5160
*261	SL " " " "	5089
262	RG earnings on 1940 unit costs	4899
263	SL earnings " " " "	4900
264	Combined RG and SL	4901
268	A & B expenditures 1935-1941	4905
269	Operating expenses in connection with improvements 1935-1941	4906
270	New equipment acquired	4907
272	Overhead and local traffic	4909
273	Interchange	4910
280	Debt to RFC	4923
Bureau of Accounts Report dated July 29, 1936		723
Bureau of Accounts Report dated December 22, 1936 and I.C.C. order thereon of January 9, 1937		5317
Bureau of Valuation Report dated March 1, 1937 and I.C.C. order thereon of March 8, 1937, Facing page and pp. 1-6		830

Number	Subject Matter	Beginning at C.C.A. Tr. p.
	Exhibits from District Court Hearings in July-August, 1940, on Old Plan	
Debtor 1	Reproduction cost	4520
" 5	"Value" of properties	4524
Insurance Group 19	SL income account 1927-1939	4531
Insurance Group 21	" annual report for 1937	4540
" " 22	" " " 1938	4562
" " 23	" " " 1939	4584
" " 24	RG " " " 1937	4608
" " 25	" " " 1938	973
" " 26	" " " 1939	4646
Guaranty Trust Ex. 2A-E	Traffic density figures 1935-1939	4689
" " " 3 (sheets 3 and 4 only)	Utah Fuel data	4700
Guaranty Trust Ex. 5	Traffic density for SL-SLW	4708
	Exhibits from District Court Hearings in October, 1942, on Interest	
Ex. 1	A&B expenditures 1936-1942	5011
" 2	RG income account 1941-42	5012

" 3	RG cash at Dec. 31, 1942	5013
" 4	RG depreciation charges	5014
" 5	SL income account 1942	5015
" 7 (only the first column and the last 2 columns of second sheet—entitled "Present and Projected D&RGW Annual Equipment, etc.")	Equipment depreciation and disbursements 1942-1955	5017
Ex. 8	Average earnings 1930-1941	5019

Exhibits from District Court Hearings in April, 1943, on Rental

Salt Lake Western Ex. 1	RG balance sheet Dec. 31, 1942	5050
" " " " 2	" income account 1942	5052
" " " " 5	Payments by RG under SL trackage contract 1940-1942	5055
" " " " 7	SL financials for 1942	5057
*Insurance Group " 3	SL annual report for 1941	5113
* " " " 4	" " " " 1942	5137
* " " " 6	RG " " " 1941	5198
" " " 7	" " " " 1942	5237

Exhibits from District Court Hearing in August, 1944, on Confirmation of Plan

*C.B.F.T.Co. Ex. 8	RG Annual Report for 1943	II 353

EXHIBIT C—CONTINUED

Number	Subject Matter	Beginning at C.C.A. Tr. p.
Exhibits from District Court Hearing on November 15, 1944, on Improvements		
Dec. 28, 1944 statement (2 pages) entitled "Statement of Charges under Reorganization Plan after Adjustment Account Purchase of Rio Grande Junction Bonds" with Clerk's note	Estimated Jan. 1, 1945 net current position and requirements	II 458-9
Exhibits before C.C.A. by its Order of January 17, 1945		
*Rio Grande annual report for 1935		II 1
*Rio Grande "Income Account, Statement of Revenues and Expenses, etc." dated August 25, 1944		II 345
*Rio Grande "Income Account, Statement of Revenues and Expenses, etc." dated Jan. 25,1945		III 547
*Rio Grande "Income Account and Financial Exhibit" dated February 3, 1945		III 560
*Salt Lake Annual report for 1943		III 573
*Salt Lake "Income, Profit and Loss, and General Balance Sheet, December 31, 1944"		III 557

Endorsed on cover: File No. 49,981, 49,982, 49,983, 49,984, 49,985, 49,989, 49,994. U. S. Circuit Court of Appeals, Tenth Circuit. Term No. 278. Reconstruction Finance Corporation, Insurance Group Committee, Central Hanover Bank and Trust Company, Petitioners, vs. The Denver and Rio Grande Western Railroad Company, et al. Term No. 279. Reconstruction Finance Corporation, Insurance Group Committee, Central Hanover Bank and Trust Company, Petitioners, vs. The Denver and Salt Lake Western Railroad Company, et al. Term No. 280. Reconstruction Finance Corporation, Insurance Group Committee, Central Hanover Bank and Trust Company, Petitioners, vs. City Bank Farmers Trust Company, Trustee, et al. Term No. 281. Reconstruction Finance Corporation, Insurance Group Committee, Central Hanover Bank and Trust Company, Petitioners, vs. The Denver and Rio Grande Western Railroad Company et al. Term No. 282. Reconstruction Finance Corporation, Insurance Group Committee, Central Hanover Bank and Trust Company, Petitioners, vs. Guy A. Thompson, Trustee, et al. Petitions for writs of certiorari and exhibit thereto. 278-282 Filed July 30, 1945. 286 Filed August 1, 1945. 291 Filed August 3, 1945. Term No. 278 O. T. 1945. 279 O. T. 1945. 280 O. T. 1945. 281 O. T. 1945. 282 O. T. 1945. 286 O. T. 1945. 291 O. T. 1945.

Table of Contents

OPINIONS BELOW 1

JURISDICTION 2

QUESTIONS PRESENTED 2

STATUTE INVOLVED 3

STATEMENT 3

REASONS FOR GRANTING THE WRIT 11

CONCLUSION 25

No.s 278 - 282

IN THE

Supreme Court of the United States

October Term, 1945

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

(And Other Cases as Shown on page i)

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

HUGH B. COX
Acting Solicitor General
W. MEADE FLETCHER, JR.,
811 Vermont Avenue, N. W.,
Washington, 25, D. C.
For Reconstruction Finance Corporation

RATHBONE, PERRY, KELLEY & DRYE
ALEXANDER M. LEWIS
70 Broadway, New York 4, N. Y.
For Central Hanover Bank and Trust Company, Trustee, Rio Grande Western Railroad Company First Trust Mortgage

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TITLES OF CASES IN WHICH THIS PETITION IS FILED

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 2906 below]

SAME

vs.

THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 2907 below]

SAME

vs.

CITY BANK FARMERS TRUST COMPANY, TRUSTEE, ET ALS.,

Respondents.

[Number 3106 below]

SAME

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 3107 below]

SAME

vs.

GUY A. THOMPSON, TRUSTEE, ET ALS.,

Respondents.

[Number 3108 below]

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Key to Record References

The record as printed pursuant to stipulation for the purposes of the Petition is cited R..... except that the original Submission Pamphlet included therein is cited by its original paging as Subm. Pamph. .....

The unprinted transcript is cited as follows: *(i)* the transcript before the Circuit Court in No.'s 2906-7 below as Tr. I.....; *(ii)* the transcript before the Circuit Court in No.'s 3106-8 below as Tr. II .....; and *(iii)* the transcript of the proceedings in the Circuit Court as Tr. III.....

Petition for Writs of Certiorari to the United States Circuit Court of Appeals for the Tenth Circuit

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The Solicitor General, on behalf of Reconstruction Finance Corporation, and other counsel named below on behalf of the respective other petitioners, pray that writs of certiorari issue to review the decrees of the United States Circuit Court of Appeals for the Tenth Circuit entered on May 10, 1945, reversing orders of the District Court for the District of Colorado approving and confirming a plan of reorganization under Section 77 of the Bankruptcy Act for The Denver and Rio Grande Western Railroad Company (the Debtor) and The Denver and Salt Lake Western Railroad Company (the Subsidiary Debtor).

RFC and Insurance Group Committee are large holders of senior securities involved in the reorganization. The other petitioners are indenture trustees under senior mortgages. The questions are of general concern in railroad reorganizations touching (*i*) the relative treatment of senior and junior creditors and (*ii*) the relative authority of the Interstate Commerce Commission and the courts.

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 233) is not yet reported except in C. C. H. Bankruptcy Law Service at ¶ 55,329.

The opinions of the District Court (Subm. Pamph. 187 and R. 213) are not yet reported except in C. C. H. Bankruptcy Law Service at ¶ 54,562 and ¶ 55,008.

The reports of the Interstate Commerce Commission (Subm. Pamph. 29, 98, 113 and 151) are reported in 233 I. C. C. 515, 239 I. C. C. 583, 254 I. C. C. 5 and 254 I. C. C. 349.

JURISDICTION

The decrees of the Circuit Court of Appeals were entered on May 10, 1945. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925 (28 U. S. C. Section 347).

QUESTIONS PRESENTED

1. Whether, under the priority rule, a Circuit Court of Appeals may modify a reorganization plan under Section 77 so that, while forcing senior bondholders, in satisfaction of their claims, to take new common stock at its par value, though there is no assurance that it can ever be sold at any price approaching that amount, it makes substantial awards of cash and new senior securities to holders of old junior bonds. This question, so far as relating to cash, is presented with respect to (*i*) cash on hand at the effective date of the Plan and the time of the Commission's finding, (*ii*) cash thereafter received before consummation of the Plan and (*iii*) cash that may be received after consummation.

2. Whether, consistently with the rule of administrative discretion, a Circuit Court of Appeals, though admittedly without power to change the Commission's determination of the amount and character of the new securities, is nevertheless free to require substantial changes in the effect of the Plan by direct allocations of cash. This question also is presented with respect to cash of each of the three kinds referred to in 1. above.

3. Whether a Circuit Court of Appeals, though concluding that the Commission's "action . . . in setting up the capital structure . . . must be upheld", is nevertheless free to require substantial changes in the capital structure by:

(*i*) adding additional new junior securities because of the court's own view of future earnings;

(*ii*) adding additional new securities, apparently of senior grades, because of the periodic retirement of equipment trust obligations, in the face of an express provision in the Plan that such retirements should reduce the new capitalization by an equal amount; and

(*iii*) requiring the issuance of new securities, apparently of senior grades, that the Plan no longer contemplates since the provisions authorizing them have been excluded from the Plan in accordance with its terms.

4. Whether, despite Sections 1(28) and 77(a) of the Act and the decision in *Ecker* v. *Western Pacific R.*, 318 U. S. 448, 506 (1943), a reorganization plan under Section 77 must require collateral pledged for obligations of, but not owned by, the Debtor to be availed of before receiving new securities from the estate.

5. Whether a class of creditors, by an adverse vote, may bar confirmation of a plan, even though such creditors, as the most junior, are allotted all of the new capitalization that remains after provision for senior creditors.

STATUTE INVOLVED

The pertinent provisions of Section 77 are copied in the Appendix.

STATEMENT

1. *History of the Proceeding.*—The petition of the Debtor for reorganization under Section 77 was filed in the District Court for Colorado on November 1, 1935. After numerous hearings in 1936 and 1937 the Commission approved a plan of reorganization. For reasons not now relevant, it was disapproved by the District Court on March 7, 1941.

The Commission held another hearing in May, 1941, thereafter received certain further evidence taken in the District Court in 1942 and 1943, in addition to current financial statements,* and approved the Plan on June 14, 1943. After hearings, the District Court approved the Plan on October 25, 1943 and, after submission to creditors, confirmed it on November 29, 1944.

The Debtor appealed from both these orders. From the latter City Bank Farmers Trust Company, as Trustee for the most junior issue of bonds (the General Mortgage Bonds), also appealed. All appeals were disposed of by the court below in its opinion and decree of May 10, 1945.

2. *The Commission's New Capitalization.*—On the usual record, including detailed evidence on every factor relating to value for reorganization purposes, the Commission fixed a new capitalization. This is to consist of four classes of new securities of fairly conventional grades,** and also of (*i*) new collateral notes under which certain of these securities are to be pledged and (*ii*) outstanding equipment trust obligations to be assumed.

Annual requirements through dividends on the Preferred Stock on all securities to be publicly held or pledged under the notes are $4,487,015. This rises to a total of $6,649,449 if dividends are included on the Common at 5%.***

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*These were always available to it by stipulation: Tr. I 1967-68 and 2500.

**The most unusual feature is that the First Mortgage Bonds (due in 50 years) are to bear fixed interest at 3% and prior contingent interest at 1%. The Second Mortgage Bonds (due in 75 years) bear contingent interest at 4½%. The dividend rate on the Preferred Stock is 5%.

***This does not include equipment trust interest or interest on new securities originally provided for an issue (the Junction Bonds) since acquired by the estate.

Historical earnings are substantially less than this total. After Federal income taxes at an assumed rate of 35%, the average annual earnings for the whole period since 1920 are only $4,647,000.* After Federal income taxes as reported in those years, the corresponding figure is $5,314,000.** On either method of reflecting income taxes, nothing at all was earned for the new Common Stock in any year of the whole period except in the peak prosperity years of 1925-1930 and the extraordinary war years of 1942-1944.

In approving this liberal capitalization the Commission no doubt gave weight to new traffic sources*** and to large improvements to the property during reorganization,† but it noted a trend to serious increases in unit costs of operation†† and held that war-time earnings could not be counted on for the future.‡

3. *The Commission's Distribution of the New Capitalization.*—All the underlying bonds are required to step down, in greater or less degree, into new junior securities. For present purposes it is sufficient to observe that all but one of the underlying issues receive the major part of their claim in

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*Computed from annual statements of record (Tr. III 19-348 and 547). Minor accounting adjustments required by the Commission are reflected. The income tax rate is taken merely as an illustration and is applied as if the Plan had been in effect throughout the total period.

**Federal income taxes actually reported in the past are, of course, an inadequate measure of the future burden because (*i*) pre-war rates were lower than probable rates for the long-term post-war future, and (*ii*) the road was shielded from their impact by the deductions available under its excessive debt capitalization, which is now to be ended.

***Subm. Pamph. 158.

†Subm. Pamph. 118, 122, 157.

††Subm. Pamph. 44.

‡Subm. Pamph. 158-9.

new stock, and two of them receive between a third and a half of their claim in new Common Stock.*

The Commission, for all that, gave only a face amount of new securities equal to the old claim, finding that "compensation to the holders of these . . . issues . . . would be adequate under the provisions of the plan"** chiefly because of "the possibility of increased return permitted by the 4½-per cent income bonds, 5-per cent convertible preferred stock, [and] unlimited dividends on common stock."† There was no finding that Common dividends in any particular amount were probable or that the new Common had any particular value.

These allocations use all the new securities except about 10% of the new Common shares. This entire balance is given to the junior system issue, the General Mortgage Bonds. At its par value it equals 10% of the total claim of those bonds. The position of general creditors and stockholders was found to be without value.

4. *Utah Fuel Stock.*—The Debtor does not own the Utah Fuel stock and never has. It was pledged under one of the underlying mortgages (the Western Consolidated Mortgage) by the mortgagor company in 1901. Upon judicial sale, subject to that mortgage, in 1920, the railroad properties passed to the Debtor (then newly incorporated to receive them) and the equity of redemption of the Utah Fuel stock passed to The Western Pacific Railroad Corporation and Missouri Pacific Railroad Company. The latter companies, to protect their stock holdings in the Debtor in its 1924 reorganization, assigned their equity so that dividends on the Utah Fuel stock should be paid to the Debtor as long

*The details appear at Subm. Pamph. flyleaf.

**Subm. Pamph. 169.

†Subm. Pamph. 168.

as certain bonds should remain outstanding, but not thereafter, the assignors reserving "the ultimate beneficial interest".*

The Plan leaves the Utah Fuel stock subject to disposition under the Western Consolidated Mortgage, by distribution to the holders of those bonds, either in kind or in proceeds of sale.**

5. *Junction Bonds.*—A section of the main line is owned by a subsidiary and leased to the Debtor. For the bonds outstanding on that section the Commission awarded $2,758,333 of new First's and Income's. But the Commission's jurisdiction over those bonds had been questioned, for the subsidiary was not a party to any proceeding under Section 77. To avoid any delay of the Plan by controversy in this regard, the Plan provided:

> "In the event that it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan in its application to the other interests, the judge may order consummation of the provisions of the plan other than those applicable to the distribution of securities to the Junction bondholders and the Junction consolidation." (Ct. R. 10,141; Subm. Pamph. 2)

This controversy was renewed in the District Court. By an order of September 16, 1943, it caused the Debtor's Trustees to purchase, and hold, the Junction Bonds.

The Commission construed this order as an exercise of the reserved power to exclude the Junction Company from

*Tr. I 3171, at p. 4. In event of foreclosure of the indentures securing those bonds, the equity of redemption was to be sold and the proceeds to be applied to payment of those bonds, any surplus to be divided among the assignors (*id.*, Article Fifth).

**Subm. Pamph. 20-21.

the Plan and thus did not submit the Plan to the holders of the Junction Bonds for their acceptance or rejection.*

The Plan provides that the amounts of new securities shall be:

> "... subject to reduction ... as equipment obligations or *other liabilities* are paid or reduced ..." (Subm. Pamph. 94, italics added.)

City Bank moved the District Court to require redistribution of the securities originally provided for the Junction Bonds, or, failing that, to disapprove the Plan on that account. Both motions were denied.

6. *Equipment Obligations.*—After the effective date of the Plan on January 1, 1943, the Debtor's Trustees continued to meet the serial maturities of outstanding equipment trust obligations. Thus the aggregate amount outstanding has declined by $609,000 in each of the two years since the effective date of the Plan.

7. *Submission to Creditors.*—In accordance with Section 77(e), the Commission submitted the Plan, after its approval by the District Court, to creditors for their acceptance or rejection. It was accepted by each class except the General Mortgage bondholders, who rejected it by a substantial majority of the small proportion that voted.**

8. *Action of the Circuit Court of Appeals.*—The court below professed to follow the doctrines laid down by this Court that its task on review was at an end if there was "warrant for the action of the District Court" and that the determination of the new capitalization by the Commission was conclusive unless "it can be said as a matter of law

*Subm. Pamph. 28.

**21.6% voted and of those 79.33% were for rejection (Tr. II 158).

that the Commission used fundamentally erroneous methods of valuation or acted arbitrarily or capriciously," thus concluding:

> "An examination of the entire record leads to the conclusion that the action and the conduct of the Commission in fixing the valuation and setting up the capital structure is free from these infirmities, and that its action in relation thereto must be upheld." (R. 245)

When it came to dispose of the case, however, the court below so far departed from these doctrines as to reverse the orders approving and confirming the Plan and to require substantial increases in the total distribution made by the Plan, both in cash and in new securities. The court thus felt free to substitute its judgment on such matters for that of the Commission. Each of these modifications also depends on the assumption that senior creditors are paid in full when they receive new securities in face amounts equal to their claims, even though such securities are largely of junior grades, indeed largely new Common Stock that offers no assurance of ever being marketable at any price approaching its par value. This assumption was made without any basis in administrative action, for the Commission found only that the senior creditors were, in the whole context of the Plan, compensated adequately to legalize the limited participation by junior interests provided for therein. The specific decisions were:

1. In the view of the Circuit Court, taken in the face of the Commission's implicit findings and apparently without regard to the requirements for a fair return on the new securities after the effective date of the Plan, net current assets are excessive, so, on the above assumption of full payment of senior creditors, all such

"excess current assets" "must be distributed" among the General Mortgage Bonds, apparently by direct award of cash from the estate (R. 247-9).*

2. As a matter of the court's own appraisal (made without apparent reference to the mounting burden of unit costs), "excess war profits" would continue for the rest of the war period** and, though the Commission was entitled not to capitalize them, it must, on the above assumption of full payment of senior creditors, provide for the distribution of such profits to the General Mortgage Bonds. (R. 247-9)

3. As a matter of the court's own independent judgment, future earnings (apparently of the long-term post-war future) will probably be "greater . . . than anticipated in the plan" and "if such should be the case, they certainly belong to the General Bondholders and not to the Seniors, and the plan should bring this about." Accordingly, "an additional amount of a subordinate stock which would receive returns only from excess dividends" is suggested as the means to remedy the asserted defect, though the choice of means is left to the Commission. (R. 249-50)

4. "The value behind the securities" provided for the Junction Bonds, as the court enigmatically put it, must, since the Junction Bonds had been acquired and "the

*The words of the Circuit Court are not beyond the reach of question, but they seem to contemplate a distribution in cash, and that interpretation is reinforced by the court's holding that current assets, even if "excessive", need not be reflected in increased capitalization.

**As a matter of fact, Gross Income in the war years has been:

1942	$17,444,000
1943	12,305,000
1944	10,912,000

Source: Tr. II 353 (at p. 19) and Tr. III 556 (at p. 5).

Senior Bondholders had been satisfied in full", be given to the General Mortgage bondholders. (R. 251)

5. Since equipment obligations had been reduced by $1,218,000 in the two years following the effective date of the Plan, "the new securities set apart for the payment of this sum [actually the Plan provides for assumption without the issuance of new securities] will not be needed" so the "unused value" behind them must, the senior bondholders having already "been fully compensated", be given to the General Mortgage bondholders. (R. 251)

6. The value of the Utah Fuel stock, though not the property of the bankrupt, must be deducted from the total claim of the Western Consolidated Bonds before they receive any recognition in new securities, and, apparently, any new securities thus becoming unused must go to the General Mortgage bondholders. (R. 252-3)

7. The General Mortgage bondholders were, therefore, "reasonably justified . . . in rejecting the plan" (R. 253).

REASONS FOR GRANTING THE WRIT

Question 1.

PRIORITY RULE

(a) Distribution of Cash.

The criterion of "fairness" in reorganization plans has a manifold impact on the national economy. It governs the character of plans for reorganization of railroads under Section 77 and of other corporations under Chapter X of the Bankruptcy Act, 11 U. S. C. §§ 501-676. In doing so it measures the protection that will be received by senior creditors, who have agreed to forego any extraordinary profits in reliance on their right to be made whole in an actual and

realistic sense before any provision is made for junior interests. Since the criterion has that critical function in the final evaluation of securities, its actual effect, as distinguished from the words in which it may be proclaimed, will affect the flow of new capital and the terms on which it may be available.

There could be no precedent more obstructive to the general public interest in the orderly completion of the remaining reorganizations in this cycle, or of others in the future, than an award of cash to junior creditors while senior creditors are compelled to take new securities, in large part of junior grades and of doubtful value. Cash is a more certain means of payment than any new security. To the extent of the cash distributed, such an award transfers the risk of ultimate satisfaction from the junior creditor to the senior, in direct contradiction of the classic priority rule.

Read in its application to the facts of this case, the precedent becomes still more alarming, for it can be rationalized only on a mechanical rule of thumb that whatever may be the principal amount or par value of new securities is equivalent to a payment in cash of that amount. There is no pretense of any finding that the new Common Stock may be sold, now or at any foreseeable future time, at anything approaching its par value. Nor is there any evidence to assure such a result. The when-issued market appraises the new Preferred at about two-thirds its par value and the new Common at about one-third.* So on the basis of when-issued quotations, none of the underlying bonds that receive any of the new Common Stock will receive, from the aggregate of the

*Judicial notice of such matters may properly be taken: *Wallace* v. *Franz*, 68 F. 2d 313, 314 (C.C.A. 8, 1933), *In re Chicago, Milwaukee, St. Paul & Pacific R.*, 124 F. 2d 754, 762 (C.C.A. 7, 1941), aff. 318 U. S. 523, and *In re Chicago and North Western R.*, 126 F. 2d 351, 367 (C.C.A. 7, 1942).

new securities allotted them, as much as two-thirds of their total claim.*

The court below goes still further. It requires all net current assets presently on hand in excess of operating requirements, and all future prosperity earnings, to be channeled off to junior interests. This is in the face of the fact that it is only from such sources that the Commission's finding of adequate compensation to senior interests by the "possibility of . . . unlimited dividends" can ever be vindicated.

The decision below represents an abrupt departure from the realism of analysis on which this Court has insisted, into a jurisprudence of symbols where proposed securities are automatically the equivalent of cash at their stated value, irrespective of their nature and quality. This is the untenable premise on which the court awards cash to junior interests. The error of that premise deepens when it is followed, as here, without regard to, and indeed against the indications of, the earnings record. Its consequence, finally, is sheer confusion when the assets and earnings which alone might support such a value are diverted to others. So these three successive steps into error are of cumulative effect and threaten to unsettle the foundations of the full compensation doctrine.

This Court thus has an opportunity, in a clear and concrete setting, to give specific meaning to the generalized expressions in which full satisfaction of senior creditors' claims has heretofore been proclaimed as a condition precedent to lawful recognition of junior interests, and to illustrate the actual working of the criterion that determines when full satisfaction is received. Without such clarification the decision below may lead to serious abuses.

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*Computed on the basis of the peak prices recently reached. On the other hand, the District Court, speaking, as the context shows, of the long-term future rather than the exceptional conditions of war-time, said that the new Common Stock "has little or no value" (R. 220).

In another respect also Question 1. (a) presents a problem of public importance. It is one that has not been, but should be, settled by this Court. Section 77(e) provides that for the purpose of *excluding* junior classes, reorganization value and permissible capitalization shall be determined as of "the time of the finding" by the Commission. The obvious purpose was to provide some fixed date, like that of a foreclosure sale, as of which such determinations should be made, for the history of rate litigations moving forward to a new point of computation at each new stage of the proceeding* haunted the draftsmen of the Act.** By that token the same date must control for the purpose of *limiting* the realization of junior classes.† It was not competent, therefore, for the court below to consider the amount of working capital *after* the date of the Commission's finding, or any increase of working capital after that date, for the purpose of inquiring whether it included any sum that could be prudently distributed to creditors of any class. To do so is to defeat the Congressional purpose which is importantly related to the practicability of the whole reorganization process. The matter is of public concern not only from that point of view, but also for due recognition of the priority rule, because from the effective date of the Plan†† all earnings must be deemed applicable to the new securities provided for in the Plan.

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*See *McCart* v. *Indianapolis Water Co.*, 302 U. S. 419 (1938) and cases cited at p. 435, footnote 19.

**Cf. Hearing before the Committee on the Judiciary, House of Representatives, 74th Congress, First Session, on H. R. 6249, April 15, 1935, p. 8, et seq. and 316 et seq.; Craven and Fuller, "The 1935 Amendments of the Railroad Bankruptcy Law", 49 Harvard Law Review 1254, 1268-76 (1936).

†Were there to be implied any exception where changes of condition are so revolutionary as to void the plan in its entirety, that would surely not be applicable here.

††So close in time (January 1, 1943) to the time of the Commission's finding (June 14, 1943) that no significant change of fact intervened, and the two dates are therefore interchangeable for present purposes.

Clarification of these points would materially facilitate the administration of the Act.

So far, finally, as the court's opinion relates to earnings to be received after consummation of the Plan, it necessarily modifies the new capital structure itself (a question dealt with in 2. below), for distribution of such earnings can not be made except by first issuing some form of new security that would evidence the right to receive and would legalize the distribution as a matter of corporate practice.

(b) Distribution of New Securities.

The questions raised by the Circuit Court's award of cash to junior interests are also raised by its apparent award to them of new senior securities. In view of the action of the Debtor's Trustees in applying cash on hand after the effective date of the Plan to the payment of equipment obligations and the purchase of the Junction Bonds, the Circuit Court, again assuming full payment of senior claims, required that "The value behind these securities" be distributed to the General Mortgage bondholders. While these words are enigmatic ostensibly they contemplate that the package of new senior securities in question be delivered to the General Mortgage bondholders, for the full "value" behind those new securities would not be distributed by the delivery of other new securities of junior grade.

If the recipients of new securities under the Plan are entitled to the benefit of all cash on hand at its effective date and all cash arising from later operations, as we believe the Act intends, they are equally entitled to that benefit whether the cash remains on hand or is invested in property improvements or is applied to reduction of debt. This is the rule applied in the important Rock Island reorganization.*

**In re Chicago, Rock Island and Pacific R.*, D. Ct. S. D. Ill., May 14, 1945, not yet reported (except in summary form in C.C.H. Bankruptcy Law Service ¶ 55,368).

The decision of the Circuit Court denies either the major or the minor premise of that fundamental rule, and further encroaches on the doctrine of fair treatment by directing, apparently, that the consequent redistribution of new securities, even though they are of senior grades, shall be wholly to the General Mortgage bondholders.

Question 2.

Commission's Discretion As To Cash

The "fair plan" that is supposed to be "The end product of this reorganization system". (*Milwaukee Case*, 318 U. S. 523, 555, 1943) and for which the approving judgment of the expert administrative agency is the first condition, would be a mockery if it covered only the distribution of new securities, without regard to the distribution of cash. That is a prime factor in fair treatment, directly for its intrinsic value and indirectly as it affects the quality of the new securities.

The amount of working capital at December 31, 1942 was considered by the Commission (Subm. Pamph. p. 155) and relied on, with current earning power, for the expectation that

> "any probable amount of cash required for paying the remaining reorganization expenses and the refunding or payment of nonassenting Salt Lake bonds can be met from funds in hand."

On that basis the Commission cancelled an earlier provision for new money. But it evidently thought that there were no surplus funds prudently available for distribution.

That administrative determination is entitled to the same respect as if dealing solely with new securities, and it should not be competent for a Circuit Court of Appeals to set it aside except for reasons justifying a change of the new capitalization, which the court below held it had no power to

make. Otherwise the basis on which the Commission relied for the fairness of the Plan may be destroyed. This Court has not previously ruled on this precise question and we submit it is of such general importance that a ruling should now be had.

The Circuit Court of Appeals for the Second Circuit has ruled on it, properly holding that:

> "It is for the informed judgment of the Commission rather than for the courts to determine the sufficiency of any cash reserve to meet the uncertainties ahead" (*In re The New York, New Haven & Hartford R.*, 147 F. 2d. 40, C.C.A. 2, 1945).

A conflict thus exists among the circuits which is particularly undesirable in a field of such general interest. It should be resolved.

Substitution of the court's judgment for that of the Commission in such matters involves special elements of hazard to the public interest, for the courts have not the experience or the facilities to exercise an informed judgment on all the pertinent facts. Thus the court below, in speaking of "excess current assets", looks only to the dollar amount of the difference between current assets and current liabilities, wholly neglecting the important factor of their ratio, which has remained almost static.* Even more importantly, the court below disregards the payments required for a fair return on the new securities from the effective date of the Plan on January 1, 1943, though it is well known that upon the consummation of other important reorganizations large cash distributions have been made for interest and dividends retroactively from the effective dates of those plans. Reflecting such a return here (even on the minimum basis of 5% Common

*158% on December 31, 1942 and 159% on December 31, 1944.

dividends),* the current position of the property would have been as follows (in thousands of dollars at December 31):

	1942	1943	1944
Current assets	$21,025	$27,266	$21,765
Current liabilities	9,560	20,033	17,055
Net current assets	$11,465	$ 7,233	$ 4,710
Current ratio	2.20	1.36	1.28

The $4,710,000 as of December 31, 1944, compares with an improvement program requirement at that time of $7,000,000 (Tr. II 451). So in fact there is a serious deficiency in net position even without any provision for working funds and reserves. The extraordinary distribution to junior interests that the court below requires will, in such circumstances, prevent the orderly operation of any plan.**

Furthermore the ruling of the court below becomes a direct modification of the new capitalization when it deals with earnings to be received after *consummation* of the Plan, and is, in that respect, covered in 1. (*a*) above as to the priority rule and in 3. below as to the Commission's function.

Question 3.

Commission's Discretion As To New Securities

When a Circuit Court of Appeals, undertaking to follow the decisions of this Court on the important matter of the distribution of authority between judicial and administrative agencies, concludes that the Commission's "action

*Source: Tr. II 353 and Tr. III 556.

**Another illustration of the dangers of a partial view is found in the emphasis given by the court below to property improvements. It spoke of them as amounting to $43,000,000, but this was without any consideration of retirements and recorded depreciation and amortization during the same period. Reflecting all these factors, the net increase in investment was only $8,000,000 from the inception of the proceeding on November 1, 1935, to the effective date of the Plan on January 1, 1943, and an equal amount thereafter to the end of 1944. Source: annual statements (Tr. III 19-348 and 560).

". . . in setting up the capital structure . . . must be upheld", and then immediately requires extensive and important changes in that capital structure, we submit it has so far departed from the usual course of judicial review as to call for an exercise of this Court's power of supervision. Unless it is recognized that the principle adverted to by the court below, which has been laid down by the decisions of this Court in areas where "It is essential that Courts regard this division of responsibility" (*N.L.R.B.* v. *Link-Belt Co.*, 311 U. S. 584, 597, 1937), is effectively nullified in practice by a decision such as that below, the Congressional scheme can not be safeguarded.

These are the changes required by the court below:

(*i*) For one it requires a diversion of all "excess" future earnings to the General Mortgage bondholders, which of course can not be arranged except by the issuance of additional new securities, and probably securities of some additional class. This the court recognized by suggesting that the means should be "a subordinate stock which would receive returns only from excess dividends" (R. 250), subordinate, that is, to the Common Stock itself, thus requiring a limitation on its dividends and changing the whole character of the new capitalization. There can be no question that through such means the dead hand of past indebtedness would effectually throttle the financing abilities of the new company, the very evil, in banker dominated days, which it was a major purpose of Section 77 to outlaw. There could be no hope of equity financing amid the deluge of paper tokens that would thus be created, even by sale of the top class of new common stock, for its chances of generous participation in the good fortune of extraordinary years would have been sapped by its parasitic inferior, and its market appeal in all years correspondingly weakened.

(*ii*) Equipment trust obligations occupy, of course, a special status, since they are not long term debt, but afford

a customary means of serial payment for new equipment, progressively with its consumption by use, from cash covered by operating charges for depreciation. The Commission, therefore, customarily provides that the approved capitalization shall be subject to reductions in such obligations.* It did so here by unmistakable terms.** No new securities of any kind were provided for these equipment obligations, but they were to be assumed by the new company. The court below, however, again asserting a power to revise the new capital structure by an original exercise of its own discretion, directs that additional new securities, of an undesignated grade, be created for the General Mortgage Bonds in an amount equal to the reduction in equipment obligations accomplished *after* the effective date of the Plan. This overrides the lawful exercise of administrative judgment on the new capitalization. In view of the nearly universal use of equipment obligations, and the continual fluctuation of their amounts, either downward by serial maturities or upward by new purchases, the decision in this respect would, if followed as a general rule, greatly obstruct the completion of reorganizations.

(iii) Since the provisions of the Plan allotting new senior securities to the Junction Bonds have, upon the purchase of those bonds by the estate, been excluded from the Plan pursuant to its terms, there are no authorized but unused securities to redistribute, and in addition the Plan provides that the capitalization contemplated by it shall be "subject to reduction . . . as equipment obligations or *other liabilities* are paid or reduced." The Commission's caution in this re-

*E.g., *Chicago & North Western Railway Company Reorganization*, 239 I.C.C. 613, 628 (1940); *New York, New Haven & Hartford Railroad Company Reorganization*, 257 I.C.C. 9, 34 (1944); *St. Louis-San Francisco Railway Company Reorganization*, 257 I.C.C. 399, 421 (1944).

**Subm. Pamph. 2-3.

spect is understandable in view of the fact that this is the third reorganization of the road since the last war, and the further fact that the provision was inserted at the time of approving a substantial increase in the new debt. That the final result is within the Commission's power is evident from the fact (pp. 4-5 above) that even after this exclusion, historical earnings do not provide a fair return on all the new securities. In the face of all these circumstances the court below asserts authority to require the creation of additional new securities in lieu of those formerly provided for the Junction Bonds and contrary to the apparent meaning of the Plan.

This is the first time that any court has overridden the administrative judgment on the amount of the total permissible new capitalization. This inroad on the Commission's statutory authority in such matters is aggravated by the fact that in this case the Commission, out of concern to protect all railroad security holders, had already been liberal, more so than is its general practice.* The decision below requiring a further enlargement of such capitalization has, therefore, special elements of danger, not only for this property but also for the regulatory scheme in its general operation.

Question 4.

Accomodation Collateral

Since the Utah Fuel stock is not property of the Debtor, it is not subject to disposition under Section 77, for that

*The new capitalization in this case is larger than in the average of all other important railroad cases, whether viewed in relation to the largest earnings in any year of the decade 1930-1939 or in relation to the physical values found by the Commission. The facts from which this purely mathematical calculation has been made appear in the published reports of the Commission and may be judicially noticed. The trial court, with its large administrative experience with the property, was troubled on this score, saying ". . . it is very doubtful in my mind if the new capital structure is not too large" (Tr. II 467).

deals only with "the debtor and *its* property".* The Commission, therefore, properly left the Utah Fuel stock subject to pledge under the Western Consolidated Mortgage, in this respect following the precise pattern of the Western Pacific plan. There the Commission held that the plan should be so framed as

> "in no wise disturbs or alters the rights of the Reconstruction Finance Corporation and the Railroad Credit Corporation in collateral pledged with them by parties other than the debtor" (*Western Pacific Railroad Company Reorganization*, 230 I. C. C. 61, 102, 1938, and to the same effect at 233 I. C. C. 409, 432, 1939).

Accordingly, under the Western Pacific plan (233 I. C. C. at 453), which was sustained by the Court on this very point,

> "This collateral . . . was therefore left with the pledgees with its position unaffected by any direct action of the Commission" (*Ecker* v. *Western Pacific R.*, 318 U. S. 448, 506, 1943).

The effect of the decision was that The Railroad Credit Corporation received new securities in respect of the full amount of the Western Pacific bonds held by it, without reduction because of any estimated realization from collateral pledged with it by others, and retained its full rights in such other collateral. Later the District Court in charge of the properties permitted The Railroad Credit Corporation to retain the payments received by it on such other collateral, despite the allocations of new securities made to it in the plan, because

> ". . . the market value of the [new] securities is much less than their face value . . . and it will not be able to realize thereon enough to satisfy its claim . . ."**

---

*Section 77(a), italics added.

***In the Matter of The Western Pacific Railroad Company*, N. D. Cal. S. D., No. 26, 591-5, June 21, 1944 (unreported). That is the case here, for, as shown above (pp. 12-13), the Western Consolidated bondholders receive, on the basis of when issued quotations, less than two-thirds of their total claim.

The Commission in this case scrupulously followed the Western Pacific precedent, for extra caution spelling out the powers of the pledgee rather than merely leaving them implicit as in the Western Pacific Case. In result the Western Consolidated bondholders remained free to realize on the Utah Fuel stock by future proceedings, though at that future time the owners of the equity of redemption would of course be entitled to limit any realization on the collateral so that the actual value of the total realization by the Western Consolidated bondholders would not exceed the amount of their claim.* But that is by no means to say that their allocation of new securities in the Plan must be reduced by any estimated amount of later realization on the collateral, as the court below insists, for that rule applies only to "property of the bankrupt"** and it is settled by this Court that the opposite rule applies to other property.† In cases like this it is the realization from other collateral that is limited, and not the realization by allocations of new securities from the estate.

The court below brushed these considerations aside, remarking that "There can be no question" but that the *estimated* value of the collateral must be deducted from the claim before any new securities are allocated. This is a decision so clearly in conflict with applicable decisions of this Court, and so likely, if left in effect, to blur the law on an important point of reorganization practice, as to merit review and correction.

Question 5.

Power To Confirm Despite Dissent

The decision below that the dissent of the General Mortgage bondholders precluded confirmation of the Plan is the

Merrill v. National Bank of Jacksonville, 173 U. S. 131 (1899).
**Section 1(28) of the Act, 11 U.S.C. Sec. 1(28).
†*Ivanhoe Building & Loan Association v. Orr*, 295 U. S. 243, 245 (1935).

first to that effect. Section 77(e) expressly authorizes confirmation after dissent if the court finds that (*i*) the plan "makes adequate provision for fair and equitable treatment" of dissenters, (*ii*) the rejection "is not reasonably justified" and (*iii*) the plan is fair and equitable and otherwise in accord with the statutory requirements. This power is important because it is the pivot of the Congressional scheme to eliminate private rights of veto.*

It has been urged by dissenters, and was urged here by City Bank, that the "not reasonably justified" phrase contemplates some more favorable provision than the basic canon of "fair and equitable"**. This would frustrate the purpose of the Act, for no plan could lawfully award any class more than what is fair and equitable, yet each class could veto it unless it did.

The court below does not adopt this dual standard, but leaves uncertain the exact grounds, and effect, of its decision.† The mere fact, however, that, in an area of the law so uncharted, the decision upheld a veto power without clear definition of its limits will tend to create confusion in the reorganization process.

This will be all the more obstructive because of the facts in this case that the dissenting class got all there was left after provision for senior classes and the gravamen of their complaint was that there is not more to distribute. It was the will of the Congress that permissible new capitalization should be fixed by the Commission, with an eye to the public interest, and not by dissenting security holders, whose attention may well be more narrowly focused.

---

*1935 amendment to Section 77; Hearings before Committee on the Judiciary on H. R. 6249, 74th Congress, 1st Sess., pp. 15, 33, 35.

**Thus City Bank urged that a rejection is "reasonably justified", if honest, unless "the plan is so patently favorable to 'those rejecting it' that no reasonable person could refuse to accept it" (City Bank's brief below dated February 5, 1945 at p. 56).

†R. 253.

It is of importance in the administration of the Act that the novel implications of this decision be set at rest and a trustworthy standard supplied for exercise of the power to confirm despite dissent.

CONCLUSION

The decision below is a dangerous departure from doctrines clearly settled by this Court on the priority rule and the administrative powers of the Commission in railroad reorganizations. In addition it undermines both doctrines by other holdings on related questions that are of general importance and have not been, but should be, settled by this Court.

The questions are of public concern, not alone by reason of the substantial risk the decision raises of indefinite prolongation of controversies in this case affecting the rights of many people and already enduring for ten years, but even more for its disturbing implications in the whole field of corporate reorganization, involving economic problems of recurrent character and national importance.

We respectfully submit that the writ should be granted.

Dated July 31, 1945.

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APPENDIX

Excerpts from Section 77 of the Bankruptcy Act As Amended.

(a) . . . If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose . . .

. . . . . .

(c) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders; does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the

approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) hereof. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) hereof, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or re-

ports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: *Provided,* That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan; or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further,* That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency

or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Commission shall certify to the judge the results of such submission.

Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided,* That if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this sub-section (e): *Provided further,* That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of

the preceding paragraph hereof: *Provided further*, That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the plan, he shall enter an order and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

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FEB 4

No.'s 278-282

JOINT BRIEF FOR PETITIONERS

IN THE

Supreme Court of the United States

October Term, 1945

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.,

Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

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February 2, 1946.

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Most of the references are to "R. .....", the printed Transcript of Record, or to the "Annual Reports" of The Denver and Rio Grande Western Railroad Company to stockholders (which are bound in a separate volume of the printed Transcript of Record entitled "Financial Statements").

Occasional references are made to various portions of the unprinted record on file in this Court, under the following headings:

D. Ct. Pro. ——	The printed proceedings in the District Court.
Ex. ——	Exhibits introduced before the Interstate Commerce Commission.
ICC Tr. ——	The original transcript of proceedings before the Interstate Commerce Commission.
I Tr. ——	The unprinted transcript of record in the appeals from the order approving the Plan.
II Tr. ——	The unprinted transcript of record in the appeals from the order confirming the Plan.
194 — Ct. —	Exhibits introduced in the cited year before the District Court.

INTRODUCTION

"These cases involve a plan for the reorganization of a railroad under Section 77 of the Bankruptcy Act."

The railroad, known as The Denver and Rio Grande Western Railroad, lies between Denver, Colorado, and Ogden, Utah. It is shown on the map in Appendix A.

After exhaustive hearings, in proceedings that have endured for a decade, a plan was approved by the Commission and the District Court for Colorado. The Plan reduces capitalization almost to the principal and interest of the secured debts having a first lien on some part of the property (the Senior Claims), converts much of their claim into new junior bonds and stock, allots the remainder of the new common to an issue of old bonds having only a junior lien (the General Mortgage Bonds) and finds that the old unsecured debt and stock are valueless. These results were far from welcome to the holders of the Senior Claims, for their new junior securities, allotted only in a face amount equal to their claim, were not such as to assure full payment. But the procedure for shaping a plan having been fulfilled by the action of the Commission, they supported the Plan, hoping to expedite the reorganization by this compromise. Nevertheless, the General Mortgage Trustee, whose bondholders would have received nothing on a strict assertion of the rights of the Senior Claims, appealed from the District Court's confirmation of the Plan.

The issue is whether the Circuit Court erred in requiring that the Plan be changed in various particulars for the benefit of the General Mortgage Bonds.

The Petitioners, asserting that the Circuit Court erred and the orders approving and confirming the Plan should be affirmed, represent each class of Senior Claims, either as owners of substantial portions of such indebtedness or as trustees under indentures securing it. They all join in this brief. The Respondents, defending the action of the Circuit

Court, are, principally, the General Mortgage Trustee and, less importantly, the Debtor and the Missouri Pacific Trustee, the latter as a holder of the old stock.

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 233-262) is reported in 150 F. 2d 28.

The opinion of the District Court approving the Plan (R. 187-206) is not reported. Its opinion confirming the Plan (R. 213-224) is reported in 62 F. S. 384.

The reports of the Commission (R. 1-186) are reported in 233 I.C.C. 515, 239 I.C.C. 583, 254 I.C.C. 5 and 254 I.C.C. 349.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on May 10, 1945 (R. 262). The petition for writs of certiorari was filed on July 30, 1945 and was granted on October 8, 1945 (R. 1201).

The jurisdiction of this Court rests on Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U.S.C., Section 347 (a)) and on Section 24 (c) of the Bankruptcy Act (11 U.S.C., Section 47 (c)).

QUESTIONS PRESENTED

1. *Distribution of cash on hand (p. 37 below):* Whether the Circuit Court was free to require a distribution of the cash on hand in a method counter to the provisions of the Plan.

2. *Distribution of future earnings (p. 55 below):* Whether the Circuit Court was free to require the creation of additional new junior securities, contrary to the provisions of the Plan, because of its own view of future

earnings, and to require the allocation of those securities to the General Mortgage Bonds.

3. *Equipment trust obligations and Junction Bonds (p. 82 below)*: Whether the Circuit Court was free to require the creation of additional new senior securities, contrary to the provisions of the Plan, because of the use of cash on hand after the stated effective date of the Plan to pay or purchase old senior debt, and to distribute additional value on that account to the General Mortgage Bonds.

4. *Utah Fuel Stock (p. 89 below)*: Whether the Circuit Court may require that the value of collateral pledged for obligations of the Debtor but owned by others must be deducted from the pledgees' claim before they can receive any new securities under the Plan.

5. *Power to confirm over a dissent (p. 100 below)*: Whether the Circuit Court was right in holding that the dissent of the General Mortgage Bonds precluded confirmation of the Plan.

STATUTE INVOLVED

The pertinent provisions of Section 77 are set out in Appendix B.

STATEMENT

1. Background of the Business Problem

A year after the golden spike near Ogden, Utah, completed the first transcontinental railway line in 1869, the first predecessor of the Debtor was incorporated.[1] It started building a railroad south from Denver to the Rio Grande River.[2] But obtaining passage through the Royal Gorge, it turned west into the fastnesses of the Rocky Mountains. At this time the road was narrow gauge. Its business was to serve the local lumbering and mining operations. But in 1890 one of its routes was changed to standard gauge and in 1901 it acquired control of a western connection to Salt Lake City and Ogden.[3] These events opened its way for transcontinental freight.

There are three main routes for transcontinental freight. The northern route is served by the Great Northern, the Northern Pacific and the Milwaukee. The central route is served by the Union Pacific and the Rio Grande. The southern route is served by the Santa Fe and the Southern Pacific (I Tr. 4395, 4399). The nearest competitors of the Rio Grande are the Union Pacific on the north, strongly entrenched in its strategic "Overland Route", and the Santa Fe on the south, with its through lines from Chicago to the Coast.

It was recognized at an early date that the Rio Grande could not live by local business alone, but must depend on

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[1] These historical matters appear in the Bureau of Valuation Report (I Tr. 832) and R. 250, n. 7; Ex.'s 136-7; and *Denver and Rio Grande Railroad Company*, 26 Val. Rep. 733 (1929).

[2] Hence its name, Denver and Rio Grande Railway Company reorganized in 1886 as The Denver and Rio Grande Railroad Company.

[3] The Rio Grande Western Railway Company, itself a successor in reorganization. The two companies were consolidated in 1908.

a substantial share of the highly competitive transcontinental freight. This was dramatized by its desperate commitment in 1905 for the construction of the Western Pacific in order to have its own friendly connections from Salt Lake to the Coast when control of its other western connections was acquired by the wealthy Union Pacific.[1] Though this commitment led to a receivership of the Rio Grande in 1920, in which it lost control of the Western Pacific, the economic fact remained. It has, indeed, grown still more urgent. In 1920 over 80% of the total tons carried by the Rio Grande originated on its own lines and only 7% was overhead business, that is, traffic received from one connecting road and delivered to another connecting road in a through movement.[2] By 1940 originated business had shrunk to 37% of total tons, while overhead business had grown to 25%.[3] This shift occurred in the face of a relatively static volume of total business.[4] As the District Court said of the overhead business,

> "Without this business, this railroad could not begin to support a capital structure of any size." (R. 203)

This fact is of critical importance in any judgment of the road's future. Its consequences ramify widely, but two stand out above the others.

One of these is the level of rates. Long-haul transcontinental freight carries a lower rate per ton mile than local freight (R. 850). So the decline in rate levels, in itself a

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[1] R. 533-536.

[2] Ex. 272, R. 1138.

[3] The percentage of overhead business to total business has, of course, sharply increased in the war years (R. 203), but the conditions of those years are too abnormal for use as a guide.

[4] The war years are, of course, an exception.

general trend of the railroad industry since 1921,[9] is accentuated as the proportion of transcontinental freight increases. Thus the average revenue per ton mile on the Rio Grande, which is "the basic index of the gross yield from transportation service" (R. 218), declined nearly 50% between 1921 and 1940, and the average revenue per passenger mile followed a similar course.[10] That means that the Rio Grande now has to perform nearly twice as much transportation service in order to obtain the same revenue as in 1921. The reduction from 1929 to 1940 was about 25% in freight rates, and more for passenger.[11]

The other outstanding result of increasing dependence on overhead business is the standard of service it necessitates. Though receiving less than before, the Rio Grande has had to provide more than before, or lose the business. The fierce competition for this traffic leaves no place for inferior service, as the Circuit Court had already observed in another connection.[12] Above all, this has required progressively faster schedules.

The physical situation of the road has always presented unusual difficulties to this development. It traverses one of the wildest mountain areas in the country. It threads through precipitous canyons that are periodically flooded by ungovernable torrents, tunnels under impassable peaks and surmounts the continental divide at 10,000 feet above sea level.[13] Its time tables aptly proclaim the "Scenic Line

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[9]Moulton and Associates, *The American Transportation Problem*, (1933) p. 113.

[10]Annual Reports, 1936 p. 27 and 1940 p. 27. The war years show a slight increase above 1940. (Annual Report, 1944 p. 29)

[11]Annual Report, 1944 p. 29.

[12]*Van Schaick* v. *McCarthy*, 116 F. 2d 987, 991, 993 (C.C.A. 10, 1941).

[13]Ex.'s 130-134 and 162.

of the World," running "Thru the Rockies—not around them."

In these circumstances the need for keeping step with current advances in the art of railroading has required huge expenditures through a long period of years. In the twenties, when the railroad industry made such large improvements to its physical plant,[13] the Rio Grande spent 40 million dollars on improvements, three-fourths of which was chargeable to capital.[14] Yet the Debtor entered the bankruptcy court in 1935 with its property starved by undermaintenance.[15] In the course of this proceeding the District Court has made up that deficiency and carried out another huge improvement program, disbursing 43 million dollars chargeable to capital and 10 million dollars chargeable to operating expenses in connection with improvements.[16]

There can be no doubt that the revolutionary changes in railroad service and facilities that impend, as a result of the accelerated technological advances of war-time and the intensified competition to result from the restoration of unlimited service by sea, air and highway, will necessitate further improvements. The District Court looks forward in these terms:

> "It is suggested by competent railroad authorities that the only solution for the American railroads in the coming post-war competition is to build super-railroads to meet this competition. Great improvement in

[13] Over 5 billion dollars in the period 1919-1929, though freight traffic increased only 10% and passenger traffic declined (Moulton and Associates, *The American Transportation Problem*, (1933) pp. 42 and 45).

[14] R. 738-9 and I.C.C. Tr. 807-16 (I. Tr. 2286-95).

[15] R. 534, 537, 195 and 221.

[16] R. 195 and Annual Reports, 1935-1944.

railroad plants and equipment will be required, together with many technical improvements—all at a very large cost." (R. 206).

In meeting these demands in the past the Rio Grande has been handicapped by excessive and unsuitable capitalization, which has forced repeated resort to the courts, four times indeed to the District Court below.[11] The company owning the Colorado properties was created in the reorganization of a predecessor. So was the company owning the Utah properties. The company resulting from their consolidation in 1908 went into receivership in the District Court below in 1918, upon enforcement of its Western Pacific guaranty. But only the old stock was eliminated, and the properties were conveyed to the Debtor (newly organized in Delaware for that purpose) subject to all the unwieldy bonded debt of the old company. In 1922 the Debtor was back in the District Court for further reorganization. All the old securities were carried forward. The only change was to convert two junior system issues of bonds into an equal amount of new General Mortgage Bonds (those in controversy here) and new Preferred Stock, both subject to a new system mortgage for further issues of debt. There has never been a dividend on the stock of either class, and the stipulated interest on the General Mortgage Bonds was paid for only four years.[12] Financing was wholly by bonds issued

[11]The American railways as a whole anticipate capital expenditures of 1,636 million dollars in the first three years after the war (Interstate Commerce Commission, Bureau of Transport Economics and Statistics, Monthly Comment on Transportation Statistics, Dec. 10, 1945). Intensified "competition within and among the several forms of transportation" is expected to be the "keynote of the postwar years" (59th Annual Report of the Interstate Commerce Commission, Nov. 1, 1945, p. 7).

[12]R. 539.

[13]Interest for the first 5 years (to February 1, 1929) was contingent on the needs of the property. In March, 1934, the Debtor proposed an interest adjustment plan (Ex. 43, 1 Tr. 3479).

under the new system mortgage and, later, by collateral notes. Beset in 1935 by a reduced traffic volume and the incipient rise in cost levels, the Debtor returned to the District Court like a homing pigeon.

But this rise in unit costs of operation did not pass off like a summer storm. It has continued relentlessly and is still in progress, thus raising a serious question as to future net earning capacity, on which we comment in the Argument below.

Such is the broad perspective in which the Commission addressed itself to its statutory function of determining a new capital structure realistically adapted to the earning capacity of the road and capable of serving its needs in adequate service to the public during the good years and bad of the long future.

2. The Properties

The Rio Grande lines may be thought of, simply, as a large Y, lying on its side across the Rocky Mountains (Appendix A). Its foot lies to the west at Salt Lake City and Ogden, where connection is made with the Western Pacific and other roads to the Coast. The right or southern arm ends at Pueblo, Colorado, where connection is made with the Missouri Pacific. That is the original line. The left or northern arm was developed just before bankruptcy to provide a new short route to other connections at Denver for the east, thus improving the competitive position for transcontinental traffic. It is not owned directly by the Rio Grande, but as stated below. Traffic moves over the two arms in approximately equal volume.

The greater part of the northern arm is owned by The Denver and Salt Lake Railway Company (the Salt Lake). A short connecting link is owned by The Denver and Salt Lake Western Railroad Company (the Salt Lake West-

ern).[20] The former was an independent road, reorganized in 1927 with a large bonded debt of its own,[21] and is not now in reorganization proceedings. Most of its stock was acquired by the Debtor shortly before bankruptcy, by means of an RFC loan for which the stock is pledged as collateral. The Rio Grande operates over that line pursuant to a Trackage Contract.[22] The Salt Lake Western is a petitioning debtor in this proceeding. Its line was built a short time before bankruptcy, by means of another RFC loan, for which all its stock is pledged as collateral. Its line is operated by the Rio Grande under a Lease.[23] Both the Trackage Agreement and the Lease have been affirmed by the District Court.[24]

The details of these relationships are not significant for present purposes, but their broad outline is, for the Rio Grande must pay to maintain its through route over the northern arm. If the holders of the Salt Lake Income Bonds consent to the modifications of their position proposed in the Plan, the Plan provides that the Salt Lake and the Salt Lake Western are to be consolidated with the Rio Grande, thus increasing the new bonds by 22 million dollars (at the same time reducing the new stock and eliminating the present Salt Lake and Salt Lake Western stock), though the Commission found that the increase in value of the system for the purposes of this proceeding because of including the Salt Lake and Salt Lake Western was only 11.6 million dollars (R. 159). Without such consent, there will be no consolidation, but the Rio Grande will con-

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[20]This line runs from Dotsero to Orestod, 38 miles (R. 32), and is called the Dotsero Cut-off.

[21]$2,000,000 of First Mortgage Bonds and $11,000,000 of Income Mortgage Bonds.

[22]Ex. 12, 1 Tr. 2684.

[23]Ex. 12, 1 Tr. 2791.

[24]R. 631.

tinue liable under the Trackage Contract and the Lease. The annual payments required under those two instruments total something over a million dollars, which do not appear in a statement of new fixed charges, but must be met nonetheless.[27] The Plan is discussed here on an unconsolidated basis, since that makes an adequate, and simpler, presentation.

3. Present Capitalization

Present capitalization, so far as need be considered here, may be resolved into two groups of claims: on the one hand, various issues of secured indebtedness having a first lien on some part of the property (referred to collectively as the Senior Claims or Senior Creditors, for no issues among them are presented here), and, on the other hand, the General Mortgage Bonds, being the most junior lien on the property and the most junior claim recognized in the Plan. Each class of the former is represented here by the parties to this brief, as substantial owners or as indenture trustees. The latter are represented here by the General Mortgage Trustee. Beyond these are unsecured claims in a small amount and Preferred and Common Stock, all of which may be disregarded in these appeals, for the finding of the Commission that they have no value was affirmed by the District Court and approved by the Circuit Court.[28]

The amount and security of the respective issues of secured indebtedness are generally indicated in the following table, and the details, if they be of interest, are shown in Appendices C and D.

[27] R. 1092 and 631.

[28] *Allen* v. *Trust Company of Georgia*, —— U. S. —— (1946); *Tennessee Coal Iron & R.* v. *Muscoda Local*, 321 U. S. 590, 605, conc. op. (1944); *U. S.* v. *O'Donnell*, 303 U. S. 501, 508 (1938); *National Licorice Co.* v. *N.L.R.B.*, 309 U. S. 350, 357 (1940). The Debtor and the Missouri Pacific Trustee petitioned for writs of certiorari on those issues, but their petitions have not been granted or denied.

Issue	*Lien*	*Amount* (in millions of dollars, principal and interest to the effective date of the Plan on January 1, 1943)
Western Trusts	First lien on most of Utah	20
Western Consols	Second lien on the above properties and first lien on some branch lines	22
Eastern Consols	First lien on most of Colorado and some equipment	56
R&I Bonds	First lien on some equipment and some branch lines; junior lien on the above properties	35
RFC Notes	First lien on all Salt Lake Western stock, most Salt Lake stock, some of above bonds (as shown in Appendix D) and other collateral	14
Generals	Junior lien on the above physical properties	44

Finally, a short segment of the main line in Colorado is owned by a subsidiary, the Junction Company, and is subject to the first lien of 2 million dollars principal amount of Junction Bonds.[37] At the effective date of the Plan they were publicly held and are provided for in the Plan, but since that time they have been acquired by the estate and are now held by it, thus raising one of the questions dealt with below.

4. The Proceedings Below

As already indicated, the proceedings that culminated in the approval of the Plan were unusually long and thorough. This is apparent from a glance at the formidable chronology:

[37] The line runs from Rifle to Grand Junction, 62 miles (R. 32). It is operated by the Rio Grande under lease.

Hearings	*Briefs*	*Opinions*	*Date*	*Pages*
I.C.C.			1936 Oct. 20-23	2,120
I.C.C.			1937 Feb. 16-17	596
I.C.C.			1937 Apr. 13-15	608
I.C.C.			1937 June 15-18 and 23	1,719
	I.C.C.		1937 Sept.	850
		I.C.C.	1938 Aug. (Ex'r's Report)	78
	I.C.C.		1938 Oct.	503
	I.C.C.		1938 Dec. 7 (oral argument)	240
		I.C.C.	1939 July 11	79
	I.C.C.		1939 Sept.	188
	I.C.C.		1939 Nov.	229
		I.C.C.	1940 Apr. 2	30
	D. Ct.		1940 July	73
D.Ct.			1940 July 29-Aug. 12	1,822
		D. Ct.	1940 Aug. 30	4
		D. Ct.	1940 Dec. 6	35
	D.Ct.		1941 Jan. 6-8 (oral argument)	231
	D.Ct.		1941 Feb.	74
		D.Ct.	1941 Mar. 6	16
I.C.C.			1941 May 20	272
	I.C.C.		1941 July	327
		I.C.C.	1941 Aug. 26	48
	I.C.C.		1941 Oct.	320
	I.C.C.		1941 Dec. 16 (oral argument)	152
		I.C.C.	1942 July 13	42
D.Ct.			1942 Oct. 23-24	172
	I.C.C.		1942 Sept.	118
D.Ct.			1943 Apr. 14-16	340
		I.C.C.	1943 June 14	56
			Total	11,342[25]

[25] In addition to documentary evidence before the Commission and 19,462 pages of printed proceedings in the District Court (only to August 2, 1943, but involving some duplications of the material listed above).

Thereafter the Plan was approved and confirmed by the District Court, and its orders reversed by the Circuit Court, as shown in the following table:

Tribunal	*Proceeding*	*Date*
D. Ct.	Hearing on approval	Sept. 13-15, 1943
D. Ct.	Opinion (R. 187) and order (R. 207) approving Plan	Oct. 25, 1943
D. Ct.	Appeal to C.C.A. by Debtor	Nov. 24, 1943
I.C.C.	Submission of the Plan to creditors	April 26, 1944
I.C.C.	Report to D. Ct. that Plan had been accepted by all voting classes except Generals[2]	July 4, 1944
D. Ct.	Hearing on confirmation	Aug. 30-31, 1944
D. Ct.	Opinion confirming Plan (R. 213)	Nov. 1, 1944
D. Ct.	Order confirming Plan (R. 224)	Nov. 29, 1944
D. Ct.	Appeal to C.C.A. by General Mortgage Trustee, Debtor and Missouri Pacific Trustee	December, 1944
C.C.A.	Oral argument in first appeal	Nov. 13, 1944
C.C.A.	Oral argument in all appeals	March 14, 1945
C.C.A.	Opinion (R. 233) and order (R. 262) reversing District Court	May 10, 1945
S. Ct.	Writs of certiorari granted	Oct. 8, 1945

[2] R. 265. The figures for the General Mortgage Bonds were 21.5% voting and of those 79.3% dissenting.

5. The Record Before the Commission

The record developed before the Commission in these lengthy proceedings is a complete one. It includes elaborate evidence on each of the various subjects that were mentioned by this Court in *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448 (1943),[30] as pertinent to a determination of reorganization value and the permissible amount of new capitalization. Specific applications of the evidence to the questions presented here will be noted later in the discussion of those questions. Its general scope is sufficiently epitomized by the following references:

1. *History of the System.*—Covered by an encyclopaedic report of the Bureau of Valuation (I Tr. 832) and illuminated in detail by a great mass of historical and corporate documents, as well as by the statistical material in the Annual Reports.

2. *Characteristics and Condition of the Properties.*—Shown exhaustively from many points of view, including the location of lines;[31] the weight of rail, nature of ballast and number and character of bridges,[32] grades, elevations, alignments and tunnels.[33] Particular attention was given to the two improvement programs, one in the 'twenties[34] and the other in the course of this proceeding,[35] showing the money spent and the improvements made.

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[30]Hereinafter cited as *Western Pacific Case*.

[31]Ex. 7, I Tr. 2682, Ex. 129, I Tr. 3954 and map bound in the Annual Reports.

[32]Annual Reports at p. 39 (or 41) and next footnote below.

[33]Ex.'s 130-134, I Tr. 3955-60; Ex. 162, I Tr. 4019; Ex. 163, I Tr. 4020; ICC Tr. 1397-1403, I Tr. 2421-27; ICC Tr. 1464-74, I Tr. 2449-59.

[34]ICC Tr. 518, I Tr. 2177; ICC Tr. 807-16, I Tr. 2286-95.

[35]Ex.'s 268-70, I Tr. 4905-7. See also R. 193 and Annual Reports.

3. *Traffic Experience and Prospects.* — Analyzed at length from all points of view, including the nature of the territory served and the business originating there;[36] the physical volume of business year by year moving over the system as a whole,[37] moving over the several parts of the system[38] and interchanged with the various connecting roads;[39] the character and volume of the different classes of commodities making up that business;[40] the relative position and trend of Rio Grande business in the whole transcontinental field, as affected by the opening of the Salt Lake-Western (Dotsero Cut-Off) and the Bieber Cut-Off;[41] estimates of future physical volume of traffic by classes of commodities;[42] and recent developments of war time.[43]

4. *Operating Revenues.*—Shown year by year since 1915[44] with various analyses and explanatory comments including a statement of the average rate per ton mile and per passenger mile year by year.[45]

5. *Operating Expenses.*—Shown for the same period with equal particularity,[46] including evidence of the marked increase in unit costs of operation during recent years and showing separately the amounts paid for taxes.

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[36]ICC Tr. 101-4, I Tr. 2028-31.

[37]Annual Reports, statement entitled "Transportation Statistics", appearing usually at p. 26.

[38]Ex. 21-21d, I Tr. 2830-34; 1940 Ct. Guaranty Trust Ex. 2, I Tr. 4689; 1940 Ct. R. & I. Ex. 2, I Tr. 4715.

[39]Ex. 23, I Tr. 2836 A; ICC Tr. 40-42, I Tr. 1978-80.

[40]Annual Reports, statement entitled "Classification of Freight Tonnage", appearing usually at p. 21.

[41]R. 949-52.

[42]R. 742-51; Ex.'s 118-120, R. 1104-08.

[43]R. 1016-17.

[44]Annual Reports.

[45]See *id.*, statement entitled "Revenue Statistics", appearing usually at p. 29.

[46]*Id.*, statement entitled "Expense Statistics", appearing usually on pp. 30-31.

6. *Net Earnings Available for Return on Securities.*—Shown year by year for the same period;[47] and estimated for the future normal year.[48] This period covered the whole of the prosperous 'twenties, the whole of the austere 'thirties and the most dazzling of the war-time years, 1942. By aid of that year's lower stage in the rising spiral of costs and a large income tax deduction for previous losses, the Rio Grande derived from the extraordinary war-time traffic of that year much greater net earnings than at any other time before or since. The period since Commission action, therefore, has not seen a further upsurge of earnings but a tapering off of the extraordinary earnings of war time.

7. *Elements of Physical Value.*—The original cost of the system properties, their cost of reproduction new and less depreciation and the value of lands and rights are shown by the Bureau of Valuation Report. Balance sheets show the recorded investment and there is extensive testimony for the Debtor on reproduction costs.[49]

6. The Commission's Action

The Commission weighed all this evidence, particularly the record of earnings so far as it thought there was a reasonable likelihood of their being realized in the future. In its original reports of 1939 (R. 68, 85) and 1940 (R. 110) the Commission, noting already "the steady increase in operating expenses, taxes, and joint facility rents" (R. 44), fixed the total new capitalization at 147 million dollars for the Rio Grande and the Salt Lake on a consolidated basis.[50] This sum was smaller than the total secured debt, so the Commission held the interests of unsecured creditors and stockholders were without value.

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[47] *Id., loc. cit.*

[48] Ex.'s 118-20, R. 1104-08.

[49] R. 827-33; I Tr. 2624-47, 2658-74; R. 894-949.

[50] That plan had no alternative of non-consolidation.

When the case came back to the Commission in 1941 after disapproval of the first plan by the District Court, new evidence was received as to the large improvement work of the Debtor Trustees and the operating economies resulting from it. These circumstances, the Commission found, indicated "an increase in earning power" (R. 123). But even so, the net earnings available for interest of the combined properties in 1940, when these economies had been largely realized, or in 1941, when the accelerated pace of national defense preparations had substantially increased railroad traffic, would not, if capitalized at 5% or even at 4%, produce a total new capitalization as large as the principal of the bonds (R. 118-19), or for that matter, we may now add, as large as the amount of the Senior Claims. Consideration was also given to physical values, where the Commission found a cost of reproduction less depreciation (plus value of lands and rights, provision for working capital and net additions) aggregating 156 million dollars at December 31, 1940 (R. 122). On all this evidence, but giving special weight to earnings, the Commission raised the total new capitalization by 8 million dollars and found in terms:

> "Considering the entire record, and taking into account the elements of value of the properties involved, their past and present earnings and prospects for future earnings, as well as other pertinent factors, we conclude and find that the value of the properties [of the consolidated system] for the purposes of this proceeding is $154,521,612 and that the total capitalization upon consummation of the plan should not exceed approximately that amount" (R. 124).

This figure being less than the bonded debt, the interests of general creditors and stockholders were again found to be without value (R. 119). The Commission felt unable to allow a further increase in new capitalization as requested by the General Mortgage Trustee (R. 138). After giving

the Senior Claims a face amount of new securities equal to their total claims, there remained new Common Stock for the General's at the rate of $70 par amount per $1000 bond (report of July 13, 1942, R. 138-39).

Within the statutory period for modification petitions,[51] the General Mortgage Trustee filed a petition of August 20, 1942, in which it asked a greater allocation of Common Stock, though admitting

> "that the present excellent earnings are unpredecented and may not continue, and that they are perhaps in part the result of the extraordinary war traffic over the lines of the Debtor." (R. 614).

While this was under submission the Commission received further evidence from the District Court, taken at the hearing of October 1942 on the petition of the Senior Creditors for an interest payment (which was denied) and at the hearing of April 1943 on adoption of the Lease and Trackage Agreement (which was ordered). This included the earnings for the full year 1942 and the cash position at the year end, in addition to evidence of further improvement work. Current financial statements and other material filed with the District Court were always before the Commission by stipulation.[52] On this record the Commission found (report of June 14, 1943) that

> "The present cash position and earning power of the Denver are adequate assurance that any probable amount of cash required for paying the remaining reorganization expenses and the refunding or payment of nonassenting Salt Lake bonds can be met from funds on hand." (R. 155)

In view of this the Commission cancelled a provision in its 1942 plan for new money for these purposes and payment

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[51] Section 77(d), last paragraph.

[52] R. 661, 789, 879.

of Trustees' certificates (actually paid later that year), and was thus able to increase the Generals' allocation to $146 par amount of new Common per $1000 bond (R. 155 and 163), or slightly more than double the previous allocation. It found, however, that there should be no further increase in new capitalization (R. 162), remarking that:

> "The debtor's earnings in 1942 are recognized, but the uncertainties surrounding the economic situation negative any assurance of a long continuation of such earning power." (R. 158-9)

The Commission thus reaffirmed its previous findings of value and permissible new capitalization:

> "After consideration of the foregoing and all the information of record, we conclude that the value of the combined properties [including the Salt Lake and Salt Lake Western] for the purposes of this proceeding is approximately $155,173,127 and that the capitalization of the reorganized system should not exceed approximately that amount.
>
> ". . . The resulting new total capitalization of the Denver [excluding the Salt Lake and Salt Lake Western] would be substantially $143,528,027. . .
>
> "We find that . . . the value of the combined properties for the purposes of this proceeding, excluding the Salt Lake and Salt Lake Western, is approximately $143,528,027." (R. 159)

The Commission accordingly approved the Plan (June 14, 1943, R. 1, 151).

7. Terms of the Plan

The details of the new capitalization may be found in Appendix E. As for allocations, RFC receives, in the event of consolidation with the Salt Lake and Salt Lake Western,

37.41% of its claim in new First Mortgage Bonds and the remainder in new Income Bonds, or, in the absence of consolidation, a new escrow note for the amount of its claim, secured by the Salt Lake and Salt Lake Western securities (and certain other collateral) now held in pledge and by the new securities issuable for the pledged Rio Grande bonds. The underlying Rio Grande bonds receive, with or without consolidation, new securities in the following percentages of their total claim as of the stated effective date of the Plan on January 1, 1943:

	First's	Income's	Preferred	Common
Western Trusts	73.5	26.5		
Western Consols		20.0	73.0	7.0
Eastern Consols	23.8	16.2	24.0	36.0
R. & I's	17.7	11.3	22.0	49.0

As stated above the Generals receive $146 par amount of new Common per $1000 bond (aggregating 10% of all the issued Common) and, as before, the interests of unsecured creditors and stockholders are found to be without value.

8. The District Court's Action

Before the District Court the General Mortgage Trustee renewed its argument that the new Common Stock issue should be increased and the whole of the increase be given to the General's (I Tr. 5280). The court, however, rejected this argument and approved the Plan. In its opinion the court stressed the competitive necessities of the property (R. 190), paralleled as it is by the Union Pacific on the north and the Santa Fe and Southern Pacific on the south (R. 204), necessities that are certainly not reduced by its increasing dependence on transcontinental business (R. 203-4) or made lighter by the exceptional severity of its operating conditions (R. 197). The huge expenditures during

the proceeding had made up the deferred maintenance of 1935 and "placed the property for the first time in a competitive position with other transcontinental carriers" (R. 196). But further improvements would be needed (R. 195-6, 197, 206). War earnings, the court found, were "inflated" (R. 192), 60% or more of passenger and freight business being due to the war effort:

> "It would, therefore, seem that very little, if any, of these inflated earnings are sufficiently permanent to form a basis for additional securities." (R. 194)

The court concluded that:

> "there is sufficient evidence to support the findings of the Commission, and . . . legal standards have been followed." (R. 203)

So it approved the Plan (R. 206).

Before the Commission an argument had been made that since the Junction Company, owning, as said above, 62 miles of the main line in Colorado (which are leased to the Debtor), was not a petitioner in any Section 77 proceeding, its 2 million of outstanding bonds were not subject to modification in bankruptcy. The Commission provided new bonds in the Plan for this issue but desired to avoid any delay because of the Junction situation in the accomplishment of the rest of the Plan (R. 166). So it authorized the District Court, if helpful to avoid delay, to terminate the provisions of the Plan as to the Junction and carry out the rest of the Plan as written, the stock and lease of the Junction in that event to become assets of the reorganized company (R. 2, 166). The same contention, and others of a complicated nature, arose before the District Court at the hearing on approval of the Plan. In this state of affairs the court, quoting the above provision of the Plan and a further provision authorizing the court to construe and to cure defects, directed the Debtor

Trustees to purchase the Junction Bonds out of "the excess cash" then on hand, remarking that there was an amount "that it is not necessary to carry forward into the reorganization" (R. 200; 262). Pursuant to this order (R. 264), the Junction Bonds were acquired by the estate at a cost of about $2,750,000 (R. 277) and are now held by it.

After the entry of the order approving the Plan on October 25, 1943 (R. 207), the Commission submitted the Plan to creditors for their acceptance or rejection and in July, 1944, certified the results to the District Court (R. 265). The Plan was accepted by all voting classes except the General Mortgage Bonds, which rejected it by a large proportion (79.3%) of the small minority that voted (21.5%).

A hearing was held before the District Court on August 30-31, 1944 on the question of confirming the Plan. The General Mortgage Trustee now urged:

(*i*) that the $2,750,000 of new bonds provided in the Plan for the Junction Bonds, by this time held by the estate, be redistributed among the Senior Claims and that an equal face amount of new Common Stock be transferred from the Senior Claims to the General's (R. 346-47, 645, 648-9);

(*ii*) that the new Common Stock issue be increased to provide a greater allotment for the General's (R. 647); and

(*iii*) that cash on hand should be distributed in payment of interest recognized in the Plan on Senior Claims, and an equal amount of new Common Stock be transferred from the Senior Claims to the General's (R. 646, 648-9).

The court denied all these motions and confirmed the Plan.

On the first point the court felt it did not have the power to make the requested redistribution because it would, in effect, change all the allocations in the Plan (R. 217). Considering the merits, however, it relied (*a*) on the fact that:

> ". . . the court in its treatment of the Junction Bonds did not pay off a debt, but only purchased securites, thereby giving the debtor control of another railroad property, to-wit, the Rio Grande Junction Railroad Company—a necessary part of its system" (R. 216);

and (*b*) on the provision of the Plan that the new capitalization should be

> ". . . subject to reduction . . . as equipment obligations or other liabilities are paid or reduced." (R. 217)

On the second point the court felt that the past history of the property left no possibility of an increase in new capitalization (R. 218). The earnings of war years, it emphasized, were abnormally inflated, 60% of gross revenues being due to war business (R. 220). This resulted not only from "the tremendous increase in total transcontinental traffic due to the war in the Pacific," but to virtual elimination of competition from other agencies of transport (R. 219). These benefits were accentuated by the more even flow of traffic occasioned by the heavier westbound tonnage of war-time, which overcame the operating handicaps of normally predominant eastbound tonnage (R. 219). All three circumstances were temporary and would end with war conditions (R. 219). The new industries of war-time in the territory were closing, except two (R. 220). Looking, then, to the long future, the court properly gave weight to two fundamental factors, "the steady and material reduction in average revenues per ton mile" and the "very large increases in operating expenses . . . greatly increased operating costs, such as wages, fuel, materials and supplies of

all kinds" (R. 218). Most significantly, the court found that these increases were of such extent as "more than offsets the economies effected by the Improvement Program" (R. 218-219). In conclusion the court felt that the new Common Stock "has little or no value" (R. 220), or if any, then wholly because of the improvement work and increase of current assets (R. 222).

The objection of the General Mortgage Trustee that cash should be distributed before the Plan could be confirmed was not pressed in oral argument, or separately dealt with in the opinion, but was overruled, with all other objections, in the order that was entered confirming the Plan (R. 224).

9. The Circuit Court's Action

The Circuit Court reversed the orders approving and confirming the Plan. One judge concurred only in result, with a separate opinion which is principally an attack on prospective earning capacity as a criterion of reorganization value (R. 254).[32] We think no further comment on that opinion necessary.

The majority opinion falls into two distinct parts, what it said, and what it did. In the former, the court concluded that the Commission had proceeded properly in setting up the new capital structure and its action in that regard must be upheld. In the latter, the court required important changes in that capital structure.

As for what it said, the court agreed with the Commis-

[32] Attention had been invited to the decisions of this Court establishing that criterion as a cornerstone of reorganization law (*e. g.*: *Consolidated Rock Products Co.* v. *DuBois*, 213 U. S. 510, 525-6 (1941); *Western Pacific Case*, 318 U. S. at 483; *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul & Pacific R.*, 318 U. S. 523, 539-41 (1943) [hereinafter cited as *Milwaukee Case*]) and to previous opinions of the same judge approving the same criterion in equity practice (*Teinmer* v. *Denver Tramway Co.*, 18 F. 2d 226, 229 (C.C.A. 8, 1927); *New York Trust Co.* v. *Continental & Commercial Trust & Savings Bank*, 26 F. 2d 872, 874 (C.C.A. 8, 1928)).

sion and the District Court that the earnings of war-time were "abnormal" and "inflated," saying:

> "These earnings are to a great extent artificial, and will disappear largely with the coming of the peace. They have very little value in estimating the probable future earnings of this property in the peace economy which is to come." (R. 242).

Moreover, it was "in the outer realm of speculation" what revenue, if any, might be derived after the war from industries opened in the territory during the war, and the Commission did not err in failing to give greater recognition to these possibilities (R. 242). Prospective earning capacity is a proper criterion of reorganization value, indeed "the only method which can insure the continued operation of a railroad without recurring receiverships" (R. 241) and that criterion was properly applied by the Commission to a long period of years, including not only depression years but normal years and abnormal war years as well (R. 242). Nor did the Commission err in refusing to increase its 1939 figure for permissible amount of new capitalization by the full amount of intervening improvements to the property: the question still was how much the enterprise could probably earn in the future; operating costs had increased; and it was quite possible that, without such improvements, "the probable earning capacity would have been substantially reduced." (R. 244) Current assets need not be reflected in new capitalization (R. 243, 246). Thus the court concluded:

> "Courts may interfere with the capital structure or valuation made by the Commission in a proceeding under this Act only when it can be said as a matter of law that the Commission used fundamentally erroneous methods of valuation or acted arbitrarily or capriciously. An examination of the entire record leads to the conclusion that the action and the conduct of the

Commission in fixing the valuation and setting up the capital structure is free from these infirmities, and that its action in relation thereto must be upheld." (R. 245)

Finally, the court noted that:

> "On appeal, our scope of review is more limited than even that of the District Court. We inquire only to ascertain whether the District Court performed its judicial functions under Subsection (e) and whether its conclusions find support in the record. We may not reverse the District Court merely because we would have reached a different conclusion. As stated by the Supreme Court, 'If there is warrant for the action of the District Court, our task on review is at an end.'" (R. 245-46)

After these orthodox pronouncements, the court moved into the second part of its opinion, the area of action. Here a different philosophy prevails. The court evidently considers that it is entitled to exercise its own independent judgment on matters of relative value, on the cash needs of the property and on future earnings.

The governing premise of the actual decision is rooted in the first of these, the matter of relative values. Here the court declares that, by the receipt of an equal face amount of new securities, though in most instances of junior grades and largely Common Stock,

> "The Senior Bondholders were *paid in full.*" (R. 247, italics added.)

Passing then to the second point, the cash needs of the property, the court holds:

> "The Senior Bondholders were entitled to receive in addition to the full amount of their claims [*sic*], working capital sufficient for proper and efficient operation of the railroad. But anything in excess of what was reasonably necessary for this purpose constituted assets

> of the insolvent corporation which *belonged to the remaining creditors.*" (R. 247, italics added)

"*We* think it is apparent," the court says,[54] in an evident exercise of its own original judgment, that there were

> "current assets on hand consisting of cash and securities in excess of what was needed for the efficient operation of the road." (R. 247)

Moving on to the third point, the course of future earnings, the court again calls on its independent judgment and prophesies that large war earnings will continue "for a reasonable time" (R. 247).

Thus as a result of all three points the court concludes that two changes must be made in the Plan, first, as to cash on hand, and, second, as to future earnings of the war period:

> "We think any plan which fails to take this into account and which gives the Senior Bondholders their claims in full by substantially delivering the road to them, and gives them the surplus cash actually on hand and further enables them to receive in addition the excess war profits which are reasonably sure to come, is inherently inequitable and unfair, so long as there are classes of creditors whose claims are not fully satisfied."[55]

Gaining confidence from this initial exercise of its independent judgment on future earnings in the particular period of war-time, the court now advances to the unlimited period of the long future. Heedless of the "outer realm of speculation," where it had said the post-war traffic of new industries lay (R. 242), and the "increased cost of operation", which it had so rightly stressed at an earlier point (R. 244), the court now requires a third change in the Commission Plan:

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[54] R. 247, italics added.

[55] R. 247. Repeated, with minor variations of form, at R. 248 and 249.

"We, however, feel that there is *more than* a speculative probability that these war industries which have been constructed along the system, as well as the improvements which have been made by the use of these net earnings, *might* produce greater net returns than anticipated in the plan. If such should be the case, they *certainly belong to the General Bondholders* and not to the Seniors; and the *plan should bring this about.* It could be done by issuing to the General Bondholders an additional amount of a *subordinate stock which would receive returns only from excess dividends.* This is a mere suggestion on our part, and in no wise binding on the Commission. Our duty is limited to pointing out *defects* in the plan. It is the responsibility of the Commission to correct them." (R. 250, italics added)

After requiring these three changes in the Plan, the court took up certain special issues and required three further changes in the Plan:

(*i*) Since the Senior Creditors are "paid in full" by new securities, the "undistributed value" behind the securities originally provided for the Junction Bonds (now held by the estate) must be given to the General Mortgage Bonds (R. 251).

(*ii*) Since the Senior Creditors are "fully compensated" by new securities, the "unused value" behind the "new securities" originally provided for $1,218,000 of equipment obligations now retired must be given to the Generals (R. 251).

(*iii*) The Western Consolidated bondholders, who have a first lien on the stock owned by the Missouri Pacific and the Western Pacific in Utah Fuel Company, must "credit the value of this collateral upon their claim before sharing in the securities of the reorganized company." (R. 252).

Finally, the court held that the General Mortgage bondholders were "reasonably justified" (Section 77(e)) in rejecting the Plan and the District Court was without authority to confirm it over their adverse vote (R. 253).

The court, however, approved the finding of the District Court that the old stock was without value and the order barring them from participation (R. 254). Nothing was said about general creditors, though the same result was presumably intended.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court erred:

1. In holding that the Plan must be modified so as to distribute any part of the cash on hand in any way other than according to the terms of the Plan as a return on the new securities provided for in it.

2. In holding that the Plan must be modified so as to give the General Mortgage Bonds all earnings for the future above any particular level, whether during the remainder of the war period or thereafter.

3. In holding that the Plan must be modified so as to give the General Mortgage bondholders anything because of the serial payment of equipment trust obligations or the purchase of the Junction Bonds.

4. In holding that the Plan must be modified so as to reduce the claim of the Western Consolidated Bonds by any amount for their pledged Utah Fuel Company stock before awarding them new securities.

5. In holding that the dissent of the General Mortgage bondholders precluded confirmation of the Plan.

SUMMARY OF ARGUMENT

I

THE CIRCUIT COURT ERRED IN MODIFYING THE PLAN SO AS TO DISTRIBUTE CASH ON HAND

The decisive date for this purpose is the time of the finding by the Commission. (Page 37 below.)

The Act requires that the validity of Commission action in limiting the recognition of a junior class shall be determined as of "the time of the finding" by the Commission (sub-section (e) of Section 77).

In applying that standard, the District Court may take into consideration all changes of condition to the time of its approval of the plan, or, where a class dissents, as here, to the time of its confirmation of the plan. But no later events are relevant under the Act.

The Plan was confirmed on November 29, 1944. Since the interval to December 31, 1944, was too short for any significant change, and year-end figures are more informative, that date closes the factual material by which the Commission's action is to be judged.

The concurring action of the Commission and the District Court in this case is a final determination of what the public interest permits. (Page 42 below.)

The Commission implicitly found that present and prospective cash position did not justify any change in the Plan. The District Court so held. These discretionary determinations were entitled to respect in the Circuit Court; for there was evidence to support them. Indeed, on the evidence it is clear that, so far from any surplus of cash, there is a serious deficiency. Net current assets are manifestly inadequate to provide in full for all operating needs, the accumulated improvement requirement and a fair return on

the new securities provided for in the Plan for the period elapsed since its stated effective date.

The Circuit Court had jurisdiction only to determine whether there was warrant for the action of the District Court. It erred in exercising its independent judgment on the financial needs of the property. It further erred in finding a distributable surplus.

The concurring action of the Commission and the District Court in this case is a final determination of what is required for satisfaction of private rights under the priority rule. (Page 50 below.)

It was a function of the Commission and the District Court to determine whether Senior Creditors were "made whole" (*Milwaukee Case*, 318 U. S. at 566). They rested their determination largely on the limited recognition given the General Mortgage Bonds and made no finding that the new securities would have a value equal to their face amount. The contrary was evidently their expectation, especially in the case of the new Common Stock. The District Court expressly found that it would have "little or no value" (R. 220) and, if any, then wholly because of the improvement work and the cash on hand (R. 222).

So the action of the fact-finding tribunals does not support, but indeed negatives, the premise of the Circuit Court that the Senior Creditors are made whole by the mere receipt of these new securities in a face amount equal to their claim. The Circuit Court was not entitled to exercise its original judgment on this question of value and the evidence requires the contrary conclusion.

The Circuit Court further erred in taking the view that such a value for the new Common as the residual owner of the whole bundle of assets would remain undiminished even though large sums of cash are stripped from the treasury.

The Circuit Court further erred in directing that such

cash be distributed to the General Mortgage Bonds while the Senior Creditors must take new securities, in large part of junior grades (or in directing that an equal amount of the new Common Stock be transferred from the Senior Creditors to the Generals if the cash is to go to the Senior Creditors).

II

The Circuit Court Erred in Modifying the Plan so as to Give Additional New Common Stock to the Generals.

The Circuit Court invades the Commission's function which is to fix a new capitalization consistent with the public interest. (Page 55 below.)

The Commission's determination of new capitalization, made in accord with prospective earning capacity as the primary criterion of reorganization value, is conclusive when supported by evidence (*Western Pacific Case*, 318 U. S. 448, *Milwaukee Case*, 318 U. S. 523).

Historical earnings, except in the extraordinary years of war time, which are not a reliable guide, have not been adequate to provide a fair return on the new securities provided for in the Plan.

Rising levels of unit costs have largely offset the economies from the improvement program and continue in such way as to raise a serious problem for the future.

Drastic declines that have occurred in rate levels add to the reservations with which past earnings must be viewed.

Such evidence fully supports the Commission's conclusions on the new capitalization. Indeed that capitalization is liberal, whether measured by this property alone or against the average of Commission plans.

The public interest is directly jeopardized by the increases in capitalization required by the Circuit Court.

The Circuit Court defeats the private right of creditors to full satisfaction of their claims. (Page 69 below.)

It is not enough that the Senior Creditors retain some seniority of position to junior interests, as the Circuit Court apparently thought, but they are entitled to receive realizable value in the full amount of their claims before the General Mortgage Bonds are entitled to receive anything: *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106 (1939); *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510 (1941); *Western Pacific Case*, 318 U. S. 448; *Milwaukee Case*, 318 U. S. 523.

If full compensation is to be attained in fact, such value must reflect what people will probably pay, either now or within some assured future.

The Commission and the District Court made no finding of such value, or of any particular value, but based their approval largely on the ground that the new Common Stock represents the entire residual equity and is given wholly to the Senior Creditors except for a minor participation of 10% to the Generals. The Circuit Court, by requiring a further issue of stock for the Generals, breaks down each of these justifications for the Plan, without any assurance that what it leaves the Senior Creditors will make them whole.

III

THE CIRCUIT COURT ERRED IN REQUIRING THE ISSUANCE OF NEW SECURITIES IN LIEU OF OLD OBLIGATIONS PAID OR PURCHASED SINCE THE STATED EFFECTIVE DATE OF THE PLAN AND IN REQUIRING THE USE OF SUCH SECURITIES FOR THE BENEFIT, DIRECTLY OR INDIRECTLY, OF THE GENERAL MORTGAGE BONDS. (Page 52 below.)

The estate has less cash because of these transactions and its net value is not increased.

The Plan provides that any reduction of "equipment obligations or other liabilities" should reduce new capitalization by an equal amount, and this, being within the Commission's power, is conclusive.

Those allotted the new securities under the Plan are entitled to the entire bundle of assets and their substantive right of ownership can not be abridged by a mere shift of value into successive forms, whether by exchange of one asset for another or by application of an asset to reduce a liability (*In re Chicago, Rock Island and Pacific R.* —— F. S. —— (N. D. Ill. 1945) 9).

IV

THE CIRCUIT COURT ERRED IN REQUIRING THE WESTERN CONSOLIDATED BONDHOLDERS TO REDUCE THEIR CLAIM BY THE VALUE OF THEIR LIEN ON THE UTAH FUEL STOCK BEFORE RECEIVING ANY NEW SECURITIES. (Page 89 below.)

The stock in Utah Fuel Company is pledged under the Western Consolidated Mortgage as a first lien and the R&I Mortgage and General Mortgage as junior liens. The equity of redemption, however, is not vested in the Debtor but in the Missouri Pacific and Western Pacific, who own "the ultimate beneficial interest."

Since the stock is not property of the Debtor, it is not subject to the jurisdiction of the Commission and courts under Section 77, for that deals only with "the debtor and its property" (subdivision (a) and *Western Pacific Case*, 318 U. S. at 506). By the same token it is not subject to the bankruptcy rule of proving for the net amount only, for that rule applies only to "security . . . upon the property of the bankrupt" (Section 1 (28) and Section 57 (h) of the Bankruptcy Act).

The equity rule, therefore, governs and the Western Consolidated bondholders are entitled, as in fact the Plan

provides, to receive new securities in respect of their total claim and thereafter to proceed against the pledged collateral, subject only to the limitation that their subsequent realization from the pledged collateral may not bring their total recovery above the amount of their claim: *Ivanhoe Building and Loan Association* v. *Orr*, 295 U. S. 243 (1935); *Western Pacific Case*, 318 U. S. 448; *In the Matter of The Western Pacific R.*, unreported (N. D. Cal. 1944), *aff. sub. nom. The Railroad Credit Corporation* v. *Ecker*, —— F. 2d. —— (C. C. A. 9, 1945).

V

The Circuit Court Erred in Holding That the Dissent of the General Mortgage Bondholders Precluded Confirmation of the Plan. (Page 100 below.)

A main purpose of the 1935 amendments to Section 77 was to eliminate the obstructions of private veto power by authorizing the District Court to put a plan in effect over a dissent upon finding it fair and equitable (subdivision (e)).

This is within the constitutional power of the Congress to adjust procedural forms to the evolving public need: *In re Chicago and North Western R.*, 126 F. 2d 351 (C. C. A. 7, 1942), *cert. den.* 318 U. S. 793 (1943); *In re Missouri Pacific R.*, 50 F. S. 936 (E.D. Mo. 1943); *Wright* v. *Union Central Life Insurance Co.*, 311 U. S. 273 (1940), *reh'g. den.* 312 U. S. 711 (1941); *Western Pacific Case*, 318 U. S. 448.

ARGUMENT

I.

DISTRIBUTION OF CASH ON HAND

1. The Decisive Date Is the Time of the Finding by the Commission.

One of the fundamental purposes of the Congress in originally enacting Section 77 was to provide an expeditious procedure for railroad reorganizations that would avoid the delays of prior equity practice.[36] This continues to be a matter of lively concern to the Congress.[37]

It was soon realized, however, that the Act was not likely to accomplish this purpose without extensive revision.[38] The principal difficulty was that the court could not confirm a plan until it was approved by the Commission and the Commission could not approve a plan until it was accepted by the security-holders, unless certain special steps should be taken.[39] All of these were commonly thought to involve a judicial finding of value. In result, junior securities could not be excluded without a judicial finding of value. But the complications, expense and delay of judicial proceedings on that issue were well known. They had become famous in public utility rate regulation. Their effect was to give junior security holders a practical power of veto.

The public purposes of the Congress should not, it was felt, be thwarted by such obstructions. The main purpose of the 1935 amendments, offered after long study by the Federal Coordinator of Transportation and his counsel, was to

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[36] H. R. Rep. No. 1897, 72d Cong., 2d Sess. (1933) 5, 8.

[37] Thus see S. Res. 192, introduced by Senator Wheeler on November 16, 1945, to inquire into the causes of delay.

[38] Annual Report of Interstate Commerce Commission for 1934, quoted in Hearings before H. R. Comm. on Judiciary on H. R. 6249, 74th Cong., 1st Sess. (1935) 66.

[39] Subdivision (e) and subdivision (g), clauses (5) and (6).

eliminate that veto power.[60] In this way it was hoped to give the Commission the power of going ahead.

The means chosen were two, to supply a simplified test of value for reorganization purposes and to authorize the District Court to confirm despite a dissent. The latter will be dealt with in V below. The former is pertinent here.

The test of value was realistically defined as prospective earning capacity, with an express negation of reproduction cost and other elements of physical value.[61] By this means it was hoped to avoid one source of delay in valuations, namely, that implicit in the complexities of the questions. They were emphasized at great length in the hearings,[62] *e. g.*, they were said to require the use of "3 days talking about the price of a little single item, to wit, cast-iron pipe."[63]

Another great source of delay in rate regulation was the absence of any fixed date of decision, so that the decisive date was in constant movement as time went by. As the process of regulation and review continued on its leisurely course, "the actual results of the Company's business during the intervening years"[64] were pertinent, so a new point of computation was repeatedly required.[65] However appropriate that might be under rate orders of continuing operation, there was no justification for it in reorganization, where participations had been historically fixed at the single

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[60]Hearings before H. R. Comm. on Judiciary on H. R. 6249, 74th Cong., 1st Sess. (1935) 15, 22, 25-26, 45, 66, 130. *e. g.*, "there is such a dead center that movement forward is impossible or at least extremely difficult" (25); the "possibility of getting through a plan . . . is obstructed by the necessity of a valuation of the property" (26).

[61]Section 77(e), last paragraph. Construed and sustained in *Milwaukee Case*, 318 U. S. at 539-41.

[62]Hearings before H. R. Comm. on Judiciary on H. R. 6249, 74th Cong., 1st Sess. (1935) 15, 22, 25-32, 105-8, 290, 316.

[63]*Id.*, 319. See also Craven and Fuller, *The 1935 Amendments of the Railroad Bankruptcy Law* (1936), 49 Harv. L. Rev. 1254, 1268-76.

[64]*McCart* v. *Indianapolis Water Co.*, 302 U. S. 419, 422 (1938).

[65]*Id.*, p. 435 and cases cited.

decisive moment of foreclosure sale. The House Committee itself stopped this gap by prescribing as the corresponding decisive moment under Section 77 the time of the Commission's finding. This it did by inserting in the bill the words italicized below:

> "The plan shall then be submitted by the Commission to the creditors of each class . . . and to the stockholders of each class . . . for acceptance or rejection . . . Provided, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that *at the time of the finding* the corporation is insolvent, or that *at the time of the finding* the equity of such class of stockholders has no value . . . Provided further, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, . . . that *at the time of the finding* the interests of such class of creditors have no value. . . ."[*]

The effect of this provision was that, such a finding having been made by the Commission and affirmed by the District Court, not only was there to be, procedurally, no submission of the plan to such class of creditors, but also, as a substantive matter under the fair and equitable standard, the plan lawfully might, and, indeed, to be lawful must, deny any recognition to that class of creditors. In other words, the Congress foresaw that the only way to provide a workable reorganization system was to prescribe a decisive date as of which value for reorganization purposes was to be determined. For that date it chose the time of the Commission finding and directed that particular classes of creditors and

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[*] Italics added. In the original the words "Provided" and "Provided further" are italicized. Source: compare the bill in Committee (Hearings, *supra*, p. 7) with the bill reported by the Committee (H. R. Rep. No. 1283, 74th Cong., 1st Sess. (1935) 18).

stockholders should be excluded from participation if, as of that time, the value of the road for reorganization purposes and, by that token, the permissible amount of the new capitalization, should be inadequate to provide anything for their claims.

Where a junior creditor complains, not of total exclusion, as in the situation just discussed, but of limited recognition, though he receives everything that is left after providing for senior claims, as here, the question is just the same, for in each case the attack is on the amount of the value for reorganization purposes and the permissible new capitalization. It would frustrate the Congressional scheme to hold that, while the rights of a creditor who receives nothing are determined as of the time of the Commission's finding, the rights of a creditor who receives 10% of his claim are determined as of some other date. The Congressional purpose requires that the same test be applied in each case.

The "time of the finding" by the Commission is therefore decisive in these appeals.[67]

Only one expansion of that "time" seems permissible under the Act. While it is the evident policy of the Act to entrust the Commission with the full scope of administrative finality, the Commission's action is nevertheless closely "brigaded"[68] with that of the District Court and the Commission's finding is not viewed as having operative effect until approved by the District Court. It may follow from this that the District Court, in approving a plan, is entitled to consider any changes of condition to that time. But consistently with the statutory purpose, such events should be appraised as of the time of the Commission's finding and the only question is whether they are of such revolutionary effect that no reasonable mind could, with an expectation

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[67] So stated in *Akron, Canton & Youngstown R.* v. *Hagenbuch*, 128 F. 2d 932, 939 (C.C.A. 6, 1942), *cert. den.* 318 U. S. 794 (1943).

[68] *Palmer* v. *Massachusetts*, 308 U. S. 79, 87 (1939).

of such occurrences, have reached the conclusion that the Commission reached when the Commission reached it.

In one situation the District Court must again review the merits of a plan. Where a plan, having been approved by the Commission and the District Court, is submitted to creditors and one or more voting classes dissent, as here, the District Court, before confirming the plan, must again find the plan fair and equitable. The Act directs that in this connection the District Court shall consider "all the relevant facts."[69] This does not disturb the statutory standard of the "time of the finding" by the Commission, but it does contemplate that, in the application of that standard, the District Court shall consider occurrences to the date of confirmation, just as before it considered occurrences to the date of approval.

So in each case the validity of the Commission's action is to be judged as of the date of the Commission's action. From that point of view, evidence may be considered of later changes to the time of approval, or, where a class dissents, to the time of confirmation. But no later events are relevant under the Act.

Upon confirmation by the District Court, the function of original decision by the Commission and the District Court has been completed and the only permissible function of review on appeal is to determine whether "there is warrant for the action of the District Court" (*Milwaukee Case*, 318 U. S. at 564). This limitation on appellate action is responsive not only to the specific policies of Section 77, but also to broader considerations, springing from the fuller information of the District Court and the requirements of orderly judicial procedure.[70]

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[69] Next to last paragraph of Section 77(e), discussed further in V below.

[70] *Kansas City Terminal R. v. Central Union Trust Co.*, 28 F. 2d 177 (C.C.A. 8, 1928), *cert. den.* 278 U. S. 655 (1929); *Badenhausen v. Guaranty Trust Company of N. Y.*, 145 F. 2d 40 (C. C. A. 4, 1944), *cert. den.* 323 U. S. 797 (1945).

In this case, the Commission approved the Plan on June 13, 1943, and certified it to the District Court on June 28, 1943.[71] The opinion approving the Plan was filed on October 25, 1943. The opinion confirming the Plan was filed on November 1, 1944. The order confirming the Plan was entered on November 29, 1944. Year-end figures being, as a practical matter, ordinarily more informative, and the interval here being too short for any significant change, December 31, 1944, is the date that closes the factual material which may be considered in determining the validity of the Commission's action in these cases.

2. The Concurring Action of the Commission and the District Court is a Final Determination of What the Public Interest Permits.

Cash and net current assets (including such cash) at dates near "the time of the finding" by the Commission on June 13, 1943, were as follows:[72]

Date	*Millions of Dollars*	
	Cash	*Net Current Assets*
Jan. 1, 1943	10	11
May 31, 1943	10	14
Dec. 31, 1943	13	14

All this was in line with the Commission's expectations. The 10 million of cash at the beginning of the year was of record before it, and was given weight in its Report (R. 155). The Commission estimated that cash at the end of the year would approximate 15.6 million (R. 158). The actual figure was 12.7 million[73] and apart from the unanticipated purchase of the Junction Bonds it would have been

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[71] D. Ct. Pro. 10,777.

[72] R. 606-9; R. 1189-90; and Annual Report 1943, pp. 12-13. Government obligations were less than accrued tax liability at each of the dates mentioned in the table and so are not included with cash. Here, as always, we exclude from current liabilities the notes that are provided for in the Plan (for they are not current demands).

[73] Annual Report 1943, p. 12.

15.6 (R. 277), surely a striking testimonial of the Commission's insight into the situation of the property.

These sums were, of course, far in excess of the cash fund required to protect current operations, for which between one and a quarter and two million dollars had been estimated, though at lower traffic levels (R. 155). But current operations were not the only call for cash. There were the general requirements of conservative management. These include adequate stores of Material and Supplies (listed as a current asset but in effect appropriated for the needs of the physical plant). They also include reserves for future contingencies, not only for specific potential liabilities, such as final assessment of taxes and readjustment of land grant rates (R. 282-83), but also for the inevitable uncertainties of the postwar transition, when new facilities may be imperative to preserve competitive position. In addition, the expenses of the reorganization must be met, including, in the event of consolidation, the cash payments to non-assenting holders of Salt Lake Bonds. This property, moreover, could not be viewed apart from its heavy backlog of improvement requirements (R. 157-8). And, finally, for any period after the stated effective date of the Plan on January 1, 1943, all proper charges under the Plan would, of course, have to be taken into account in order to cover accruals of interest on the new bonds and provide for dividends at the designated rate on the new Preferred Stock and a fair return on the new Common (R. 158), because those who receive the new securities are entitled to the income after the stated effective date of the Plan.

In the light of such considerations, typically within the field of the Commission's expert administrative judgment, the Commission found that:

> "The present cash position and earning power of the Denver are adequate assurance that any probable amount of cash required for paying the remaining re-

> organization expenses and the refunding or payment of non-assenting Salt Lake bonds can be met from funds on hand." (R. 155).

The Commission accordingly eliminated from the Plan its former provision for borrowing new money. But it did not think fit to do more. This action, we submit, is implicitly a finding that the present and prospective cash position were not such as to justify any change in the capitalization or allocations in the Plan. This finding is entitled to the same measure of respect by the courts as if refusing for any other reason to change the permissible amount of the new capitalization or its allocation among the old securities. It is thus conclusive if within the area of reasonable judgment, which it certainly is in this case. As the Circuit Court of Appeals for the Second Circuit said in refusing to disturb a Commission plan upon a similar attack:

> "It is for the informed judgment of the Commission rather than for the courts to determine the sufficiency of any cash reserve to meet the uncertainties ahead." (*In re The New York, New Haven & Hartford R.*, 147 F. 2d 40, 46 (C.C.A. 2, 1945)).

Granted, however, that the District Court retains considerable freedom of discretionary judgment as to the use of cash under its administration, the District Court affirmed the Commission's conclusions. It did so both in approving the Plan and in confirming it.

At the first of these times the General Mortgage Trustee objected that:

> "The Plan fails to give sufficient weight to the great improvement in the financial position of the Debtor" (D. Ct. Pro. 10,381).

The District Court overruled this objection and approved the plan (R. 207, October 25, 1943).

About a year later the Plan came on for confirmation and the General Mortgage Trustee specifically urged that "the accumulation of surplus cash" should be applied on the Senior Claims and that new securities which would not, after such payment, be needed to satisfy the Senior Claims should be redistributed to the General Mortgage Bonds (R. 645 and 648). This request also was denied by the District Court in its order confirming the Plan (R. 230).

At that time (substantially December 31, 1944) cash plus the excess of Government obligations over accrued tax liability equalled 12 million dollars and net current assets (including the cash and Governments) were 16 million dollars. This was not far from the condition at the time of the Commission's action, about one or two million more in each instance. What were the requirements to be met from those funds?

First of all, of course, there must be adequate provision for the operating needs of the property, including the cash working fund, the necessary Material and Supplies, expenses of reorganization and reserves for contingencies.

Then there must be due provision for necessary improvements to the property. The amount required for the improvement program and carry-over at December 31, 1944, was 7 million dollars (R. 1199). Those funds can not be provided from sale of new securities, for that would exceed the Commission's limits for the new capitalization at the very moment of its issuance.

Without attempting to assign any particular figure for the operating needs referred to above, it is plain that the size of the improvement requirement is such as to raise a serious question whether both needs can be provided for in their entirety. At the least it is impossible to say that there is no basis on which a reasonable mind could conclude that there is no cash surplus to distribute.

But that is not all. The Plan recognizes interest on the Senior Claims only to January 1, 1943 (its stated effective

date), and after that time intends to substitute interest accruals on the new bonds and a fair return on the new stock. Until such amounts are paid or provided, a matter to which the Circuit Court seemingly gave no attention, there can be no question of surplus funds, since not until that time will the Plan work as intended or make any approach to full compensation for Senior Claims. The rate of a fair return is fixed by the Plan for the new bonds and the Preferred Stock. For the new Common it, of course, is not. But the prospect of "unlimited . . . dividends" on the Common was expressly relied on by the Commission as a part of its basis for finding adequate compensation to Senior Creditors under the terms of the Plan (R. 167). The average rate of return on the Common should be greater than the 5% rate fixed for the Preferred in order to compensate for the greater risks of the junior position. This requires generous payments in years of unusual prosperity, substantially greater than the desired average, for otherwise the average can never be maintained at the perimeter of earnings where this new Common lies. At a 10% dividend rate on the new Common the unpaid accruals under the Plan for interest and dividends to December 31, 1944, were 15 million dollars.* At a mere average rate of 6% for Common dividends, unpaid accruals were 11 millions. Without any provision for Common dividends at all, unpaid accruals through the Preferred were 6 millions. None of these amounts can be provided for in full if the whole of the improvement requirements are to be satisfied. In these circumstances there is a very ominous likelihood that no Common dividends whatever will be paid for even these two brilliant years of 1943-1944 when, under the stimulus of abnormal war conditions, earnings soared above all pre-war peaks.

This is shown in very concrete form if we put the matter the other way and provide a return on the new securities

*This is the net figure, after deducting the interest payment of 2.4 million made in 1944 (R. 634).

before taking care of any other requirements. Allowing, for the purposes of this illustration, Common dividends at the inadequate rate of merely 5%, the current position would have been as follows (in thousands of dollars at Dec. 31):

	1942	1943	1944
Current assets	$21,025	$27,266	$21,765
Current liabilities	9,560	20,033	17,055
Net current assets	$11,465	$ 7,233	$ 4,710
Current ratio	2.20	1.36	1.28
Current ratio for all Class I railroads[35]	1.71	1.55	1.59

Thus, without any provision for operating requirements, there would have been on hand at the end of 1944 only 4.7 million dollars of net current assets to satisfy the improvement program requirement at that time of 7 million dollars. Of course no such calamitous deficiency in net position could be allowed to occur.

In these circumstances, where the current position does not even permit a fair return on the stock provided for in the Plan, we submit it is impossible to find any surplus from which debt dealt with in the Plan must be retired for the benefit of junior interests.[36]

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[35] I.C.C. Statement M-125, Selected Income and Balance Sheet Items of Class I Steam Railways in the United States, December 1943 and 1944.

[36] This situation is essentially different from that presented in the cases urged below by the General Mortgage Trustee:

In Re Florida East Coast R., 52 F. S. 420 (S. D. Fla. 1943);
Chicago, Milwaukee, St. Paul & Pacific R. Reorganization, 257 I. C. C. 223 (1944);
In Re New York, New Haven and Hartford R., 54 F. S. 595 (D. Conn. 1943), *aff.* 147 F. 2d 40 (C.C.A. 2, 1945), *cert. den.* —— U. S. ——, 89 L. Ed. 1553 (1945).

In each of those cases interest on all, or most all, of the underlying bonds had been paid in full and, at the time of District Court hearings on approval of the plan (or confirmation when a class of security holders had dissented), there was still a very large *actual surplus* of cash that, as said in the first of those cases, was "prudently available" for distribution.

So the District Court rightly had no hesitation in rejecting the request of the General Mortgage Trustee for a distribution of funds for this purpose (R. 230).

This question of the financial needs of the road was a purely factual one. The existence or extent of surplus net current assets is nothing but a question of fact. It can not be masked, in the words of the Circuit Court, as "a pure question of law" (R. 253). On such matters the Circuit Court has neither the experience nor the facilities for an original judgment. To dispose of the problem in such terms is to disregard the finding of the Commission, though uniformly entitled to finality on the facts as a matter of administrative function,[77] and the judgment of the District Court, though uniformly entitled to finality on facts of this kind as a matter of judicial discretion.[78] These general principles are adopted in Section 77, which confides the decision of such matters to the concurring action of the Commission and the District Court and limits the scope of review to the question whether "there is warrant for the action of the District Court" (*Milwaukee Case*, 318 U. S. at 564). Heedless, however, of these fundamental limitations on its appellate jurisdiction, the Circuit Court undertook to substitute its own judgment on this factual question, saying, without any review of operating needs, or improvement requirements or accruals under the Plan:

> "*We* think it is apparent from the record that there are current assets on hand consisting of cash and securi-

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[77] *E. g., I.C.C.* v. *Illinois Central R.*, 215 U. S. 452, 469-70 (1910); *U. S.* v. *Detroit and Cleveland Navigation Co.*, —— U. S. ——, 90 L. Ed. 12 (1945).

[78] *E. g., In Re Philadelphia & Reading Coal & Iron Co.*, 141 F. 2d 954 (C.C.A. 3, 1944); *In Re Philadelphia & Reading Coal & Iron Co.*, 117 F. 2d 976, 978-9 (C.C.A. 3, 1941); *Van Schaick* v. *McCarthy*, 116 F. 2d 987, 993 (C.C.A. 10, 1941); *In Re St. Louis Southwestern R.*, 17 F. S. 68 (E. D. Mo. 1936), *aff. sub. nom. Bankers Trust Co* v. *Henwood*, 88 F. 2d 163 (C.C.A. 8, 1937).

ties in excess of what was needed for the efficient operation of the road." (R. 247, italics added).

To the extent, though apparently an incidental one, that the Circuit Court relied on the District Court's observation in the opinion approving the Plan that, for the purpose of the purchase of the Junction Bonds, there was on hand "an amount of cash far in excess of the needs of reorganization expenses, including working capital" (R. 248), it misconceived the meaning of the District Court. That statement, even if not superseded by the later order confirming the Plan, did not deal with improvement requirements or with accruals under the Plan. And it certainly was not intended as a finding that there was any genuine surplus in an overall view. The same is true of the oral, and thus less exactly phrased, remark at the September 1943 hearing that the road "has an amount of cash here that it is not necessary to carry forward into the reorganization" (R. 262). The District Court's position on cash has been clear and consistent at all times. It refused to make any payment on old securities, even from the unprecedented earnings of 1942 (R. 1018), until there was an approved Plan, and then paid only such amounts as were equal to the interest that would be mandatorily payable on the new bonds at the time of their issuance (R. 634). Apart from that, the only distribution was the purchase of the Junction Bonds, which would reduce the initial debt capitalization. In other words, no distribution of cash has been made on old securities except where operating to pay or reduce the obligations of the reorganized company.

If, on the other hand, the Circuit Court was looking, as its bare words may imply, only to the cash required for current operation of the physical property, this was likewise a usurpation of the function of the Commission and the District Court. They were entitled to see that the reorganized

company is equipped not only for current operation of the physical property, but also to maintain its system as a going concern, protected against all reasonable contingencies, able to meet its improvement needs and qualified to pay a fair return on the new securities provided for in the Plan.

So the Circuit Court, we submit, overstepped the limits of its appellate power, and its decision cannot be supported on the facts. The result of its apparent direction for a substantial distribution of cash may well be to impede or prevent the orderly operation of any plan.

3. The Concurring Action of the Commission and the District Court is a Final Determination of What the Priority Rule Requires.

Up to this point we have dealt in terms of the public interest in the preservation of adequate funds for the needs of the property, referring to private rights only in so far as a fair return on the new securities marks one of the needs to be met. But in still another respect, the vital matter of determining due satisfaction of the priority rule, the action of the Circuit Court conflicts with established principles. The original determination of this question also is a function of the Commission and the District Court. This Court has said:

> "Whether in a given case senior creditors have been made whole or received 'full compensatory treatment' rests in the informed judgment of the Commission and the District Court on consideration of all relevant facts." (*Milwaukee Case*, 318 U. S. at 566)

The Commission and the District Court discharged this function, but obviously based their conclusion in large part on the limited participation permitted the General's in the Plan, the very limitation that the Circuit Court destroys. There was, as we point out more fully at page 77 below, no finding by the Commission or the District Court that any of

the new securities, and most particularly, of course, the shares of new Common Stock, would have a value equal to their face amount, that being the amount at which they were distributed in the Plan in satisfaction of the Senior Claims. Nor was there any finding of any particular amount of prospective future earnings available for dividends on the Common Stock. The Commission contented itself with the finding that "under the provisions of the plan" (R. 169), among the most important of which was the limited recognition given to the General Mortgage Bonds, so that the Senior Creditors took nearly all of what there was, the compensation to Senior Creditors "would be adequate" (R. 169). As for realizable value, it was evidently the Commission's expectation that the new stocks would sell substantially below their par amount, for it held that RFC, upon receiving its total claim in new First Mortgage Bonds and Income Bonds, was "not fully secured" (R. 178) and was thus entitled to additional amounts representing payments on its rental claim. The District Court, for its part, found in terms that the new Common Stock "has little or no value" (R. 220), and, if any, then wholly because of the improvement work and the current assets on hand (R. 222).

So the Circuit Court had no basis in any action of the fact-finding tribunals when it took the view that the new securities, even the new Common Stock, would have a value equal to their face amount (R. 247). This was a new pronouncement of its own, made *ex cathedra*, without analysis of the facts of record and without reference to any price at which the new Common Stock may be sold, either now or at any foreseeable future time. If this pronouncement purports to be an original finding by the Circuit Court, we submit that action is beyond the proper limits of its appellate function. If it is not such a finding, it is a mere assumption that new securities are automatically worth their face amount without reference to their quality or earning power. On the facts,

as we show more fully below, the historical earnings of the road give no assurance, but on the contrary make it most unlikely, that the new Common Stock will have a value equal to its par amount within any foreseeable future time (p. 50), and these indications are corroborated by when-issued market quotations, which value the new Common Stock at roughly one-third its par amount.[79] So we submit that this fundamental premise of the Circuit Court is not only unsupported by the action of the fact-finding tribunals, but indeed is contrary to their action, and, wholly apart from their action, is contrary to the evidence. The fundamental requirement for full satisfaction of senior debt cannot survive in actual practice if applied only in these paper terms. Yet it was only by such an assumption that the Circuit Court upset the Plan.

Equipped with this premise, the Circuit Court takes a further step. The value attributed to the new Common as the residual owner of the entire bundle of assets will, the Circuit Court further assumes, remain undiminished even though large sums are stripped from the treasury, so that the road is left only with such net current assets as may be essential for bare operating needs.[80] At this point it is of no concern whether there was or was not a surplus of current assets, for, however the assets may be classified, there is no doubt that they were all taken into account by the Commission and the District Court in their respective findings that the Plan is fair and equitable. It is obvious, particularly in the circumstances of this case, that the present and prospec-

[79]See Appendix G and the discussion of it on p. 80 below.

[80]Indeed, the Circuit Court thinks the assumed value will persist even if *all* net current assets are distributed, leaving only the bare bones of the physical plant; for the Circuit Court, though generously according the Senior Creditors "working capital sufficient for proper and efficient operation of the railroad", evidently thinks that would involve an *excess* recovery "in addition to the full amount of their claims" (R. 247).

tive cash position of the road was a factor, and a material one, on which the Commission based its finding that compensation to Senior Creditors is "adequate under the provisions of the plan" (R. 169). It was expressly relied on by the District Court as one of the only reasons for a value in the new Common Stock (R. 222).

So if current assets might fairly be said to include any surplus beyond the needs of the road, that surplus belongs to the Senior Creditors, as recipients of 90% of the new Common stock, and is a necessary component of their award in order to make out adequate compensation on this record and permit any participation at all by the General Mortgage Bonds. Since the Commission and the District Court viewed the property in the context of its cash resources, clearly neither one of them considered the value of the new securities apart from the cash resources and the Circuit Court was on wholly new ground when it found or assumed a value in such circumstances.

That conclusion, contrary to the evidence even with the cash in the till, is all the more so with the cash gone. It becomes a mere fantasy when the cash is to go, as the Circuit Court requires, in such amounts as to preclude completion of the necessary improvement work and make wholly impossible any approach to a fair return on the new securities from the effective date of the Plan, The priority rule under such manipulation becomes a mere matter of history.

But this does not deter the Circuit Court. It has such confidence in the concept that securities are counters of fixed value that it apparently takes still another step into error by directing that the required distribution of cash be made to junior creditors. Its words are:

> "The Senior Bondholders were entitled to receive in addition [*sic*] to the full amount of their claims, working capital sufficient for proper and efficient operation of the railroad. But anything in excess of what was reasonably necessary for this purpose constituted assets

> of the insolvent corporation which belonged to the remaining creditors." (R. 247)

In other words, all cash or its equivalent in excess of immediate operating necessities "belonged to" the General Mortgage Bonds, so, the Circuit Court concludes,

> ". . .the plan of reorganization should have made sure that all excess current assets . . . would go to the General Bondholders." (R. 249)

The General Mortgage Trustee, startled by this golden shower upon the junior creditor, says the Circuit Court does not mean what it says.[51] But its words, we think, remain the best evidence of its intention. However startling that may be, the words say that current assets shall be converted into cash and cash shall be distributed to the most junior lienor though senior lienors are compelled to take new securities, in large part of junior grades and of undeniably doubtful value. Cash is the highest medium of compensatory treatment and surely a more certain means of payment than any new security. To the extent of the cash distributed, such an award transfers the risk of ultimate satisfaction from the junior creditor to the senior, in exact reversal of the priority rule, in any form that it has ever been put.

This should certainly be rectified. But our case does not stop there. Whatever the Circuit Court may have intended as the destination for the surplus cash it conceived to exist, its intention is unjustifiable. Even if the Circuit Court intended a distribution among Senior Creditors, still its design was that an equal par amount of new Common Stock should be taken from the Senior Creditors and given to the Generals. This in itself repudiates the Commission's findings of the equitable equivalent of the present claims, di-

[51] Brief in opposition to certiorari dated August 31, 1945, p. 15.

verts value from the Senior Creditors to the Generals, and breaks down the very limitation that made the Plan legal in the view of the Commission and the District Court. It is, therefore, like the Circuit Court's other allocations of stock to the Generals dealt with in II and III below and unlawful for the same reasons because preventing full satisfaction of Senior Claims.

So the action of the Circuit Court in regard to cash on hand is erroneous from the point of view of private right as well as from the point of view of the public interest, and on both grounds should be reversed so that, in regard to cash on hand, the orders establishing the Plan may be affirmed.

II
DISTRIBUTION OF FUTURE EARNINGS

1. The Circuit Court Invades the Commission's Function which is to Fix a New Capitalization Consistent with the Public Interest.

Evidence of past earnings.—The Commission's task of shaping a new capitalization was not a problem of mere mathematics. It was an exercise of informed judgment on the probable composite result of diverse trends so fundamental as to condition the very ability of the railroads to continue under a system of private ownership. The physical volume of business and the rates to be charged are primary factors on total operating revenues. Operating costs and taxes are primary factors on what will remain for a return on new securities. Innumerable other developments condition these trends or directly affect net earnings. So the Commission's reasoning can not be exposed in a syllogism.

But the past is surely evidential for the future. And in inquiring whether there was evidence to support the Com-

mission's capitalization, the record of past earnings is informative.

The Commission had before it the earnings of the road for the whole period 1915-1942. No doubt, special circumstances typified the years before the termination of Federal control following World War I. But the remaining years supplied a broad base for an intelligent estimate of future prospects. The earnings for nearly all of two more years were before the District Court. So the whole period 1921-1944 was covered, down to what has been identified above as the cut-off date.

Under the prescribed classification of accounts, net earnings available for interest are stated after provision for all taxes, including those based on income. In that matter of income taxes, the recorded earnings available for interest in the past are greater than those to be expected in the future, first because the deductions allowed for interest on the excessive debt capitalization of the past are larger than those to be available on the reduced debt capitalization of the Plan, and next because the tax rates of all but the very recent years of the past are less than those that will probably prevail through the long future. Correction in both respects is a simple calculation once granted the applicable tax rate.

In Appendix F we summarize the earnings in 1921-1944 as applied under the Plan. On the applicable tax rate it is, of course, impossible to be precise. As a general illustration of probabilities, though in no sense an attempt at prophecy, we use a rate of 35%. But to avoid any question on such matters we then show the situation as if there were no Federal income tax whatever.

The results are that, on a 35% tax rate, dividends on the new Common at 6% have not been covered in any year of the whole period except the extraordinary war years of

1942-1944.[82] On the average through the whole period, ~~even~~ Preferred dividends have ~~not~~ hardly been covered, and the result of paying 6% dividends on the Common throughout the period would, without any use of income for improvements, be a deficit of 61 million dollars. Even in the unthinkable condition of no Federal income taxes, Common dividends at 6% would have been covered in only three additional years (1926, 1928 and 1929), and the regular payment of such dividends throughout the period would have left a deficit of 28 millions.

The calculations underlying these figures are not open to mathematical argument or question. They are the officially reported earnings, increased in a substantial amount to reflect the operating economies on the 1940 basis from the improvement program, and applied in the alternative to the approximate present level of income taxes or to a situation where there are no income taxes at all. The earnings are shown in their entirety, without any provision for improvement expenditures, though these averaged 3.3 million dollars a year in the decade 1926-1935[83] and 4.8 a year in 1936-1944.[84]

On that record, we submit, it is impossible to say that there is no evidence to support the Commission's action in fixing the new capitalization as provided in the Plan.

Earlier proposals.—The justiciable question is, of course, only whether the new capitalization actually provided for in the Plan itself is within the Commission's power. The courts do not sit to review any earlier administrative steps along the road to the final result, or the consistency or in-

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[82]The extraordinary level of operations in those years is indicated by the fact that total revenue net ton miles in 1942, 1943 and 1944 were 214.2%, 257.3% and 254.4%, respectively, of the previous peak of 1929. (The revenue per ton mile, however, was only 76.8%, 78.4% and 79.2%, respectively, of the 1929 figure.) See Annual Reports.

[83]R. 735-7 and Ex. 73 (I Tr. 3693).

[84]See Annual Reports.

consistency of the reasoning that accompanies them. This rule is rooted deep in obvious policy and applied broadly throughout the field of administrative law.[85] So the Circuit Court went astray when it gave weight to earlier proposals of the parties themselves (R. 238), for they were not admissions, but on their face mere compromise proposals,[86] and even had they been admissions, they must be deemed ineffective against the statutory command for a fair and equitable plan compatible with the public interest.[87] Nor are the General Mortgage Bonds entitled to any special regard because it took time to solve the problems of the reorganization, thus increasing the amounts due Senior Creditors by the amounts accruing for interest (R. 238, 244, 248-9). That is one of the burdens of civilization, of which all people, and particularly junior creditors, assume the risk. It was for the Commission to formulate a plan and it discharged that duty. It was not obstructed but assisted in the discharge of that duty by suggestions from the Senior Creditors and numerous compromises by them.

Property improvements.—There were questions, no doubt, for the Commission to resolve as to the weight of that evidence, such as the question stressed by the General Mort-

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[85]On the specific point of railroad reorganization plans, see *In Re New York, New Haven & Hartford R.*, 54 F. S. 595, 602 (D. Conn., 1943). As to the powers in general of the Commission and other administrative agencies, see *Virginian Railway* v. *U. S.*, 272 U. S. 658, 663 (1926, I. C. C.); *Tagg Brothers & Moorhead* v. *U. S.*, 280 U. S. 420, 445 (1930, Department of Agriculture); *N.L.R.B.* v. *Baltimore Transit Company*, 140 F. 2d 51 (C.C.A. 4, 1944); *Niagara Falls Power Co.* v. *F.P.C.*, 137 F. 2d 787 (C.C.A. 2, 1943); *Knight* v. *U. S. Land Association*, 142 U. S. 161 (1891, Department of the Interior); *Pearson* v. *Williams*, 202 U. S. 281 (1906, Immigration); *Houghton* v. *Payne*, 194 U. S. 88 (1904, Post Office Department).

[86]*E. g.*, ". . . the inclusion of this suggested compromise offer [R. 604B] is in no sense a waiver of the Committee's position on any issue." (II Tr. 141)

[87]*Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, 114, 128-9 (1939).

gage Trustee, of the economies from the large improvements to the property. But as the following comments show, these were merely matters for the Commission to appraise.

Certainly there have been large improvements during the proceeding, though the 43 million dollar figure of the Circuit Court (R. 243) does not give the full picture, since it does not reflect retirements and recorded depreciation and amortization during the same period. Reflecting all these matters the net increase in investment was only 8 million dollars from the inception of the proceeding on November 1, 1935, to the stated effective date of the Plan on January 1, 1943.[58] But the Commission was not obliged to increase the new capitalization by an equal amount. On the contrary, the question still was the amount of prospective earning capacity. The mere addition to investment does not automatically raise that level.[59] Though more recent, and thus in point of degree more persuasive than older installations, it is nevertheless relevant only in so far as it "may indirectly bear on earning capacity." (*Milwaukee Case*, 318 U. S. at 541) The Circuit Court purportedly accepts this result, observing that, without the improvements, earning capacity might have been "substantially reduced" (R. 244). It also correctly holds that the wisdom of the expenditures is not in issue here (R. 244), for that could have been raised only in appeals from the authorizing orders, and the General Mortgage Trustee never took any such appeal. But, in the face of these observations, the Circuit Court apparently allows the mere dollar amount

[58] See Annual Reports. There was a further, and equal, net increase in investment between January 1, 1943, and December 31, 1944, but this was made from funds equitably belonging to those who receive the new securities under the Plan.

[59] *Missouri Pacific Reorganization*, 257 I.C.C. 479, 525 (1944).

of these expenditures to override the Commission's administrative judgment on resulting net earning capacity.

Operating Expenses.—On the fundamental question of net earning capacity it is, of course, true that many of the improvements save expenses, as by reducing man-hours of work or unit consumption of materials and supplies. Indications of these effects were put in evidence at the last Commission hearing (R. 840, 1133-35) and are reflected in the above figures. It was largely on that basis that the Commission increased total new capitalization by 8 million dollars.[30] Without this increase, it will be noted, there would have been nothing at all for the General Mortgage Bonds. But reduction in man hours of work, or in consumption of units of materials and supplies, is not the whole story, by any means. Increases in compensation per man hour of work, or in cost per unit of materials and supplies, may leave actual costs unchanged, or even greater, and it is, of course, the actual costs and the actual resulting net that is significant. For many years one of the most pervasive and fundamental trends in the railroad industry has been a seemingly inexorable advance in unit costs. This was emphasized by the Commission as early as its first report on this reorganization in 1939 (R. 44). Since then the evidence shows that wages on this property have increased 30% and the unit costs of materials and supplies 16% (R. 300). The Debtor Trustees estimated that the 1943 wage increase alone added 2.7 million dollars to 1944 operating costs.[31] That equals a 6% return on 45 million dollars, a sum greater than the total additions and betterments during the whole time of the proceeding. It is well known that requests for

[30] Cf. R. 68, 120, 124, 159.

[31] Annual Report 1943, p. 5.

further increases are now presented and in course of consideration. The trend is evident in the following table:[92]

	000's omitted		
	1942	1943	1944
Gross Income	$17,444	$12,305	$10,912
Income taxes	2,180	7,184	5,338
Total (equivalent to earnings available for income taxes and return on securities)	19,624	19,489	16,250
Ry. Operating Revenues	54,475	70,194	70,347

In other words, despite a 15 million dollar increase in Railway Operating Revenues in 1943, the balance for income taxes and return on securities was unchanged; and on the same level of Railway Operating Revenues in 1944, the balance for income taxes and return declined 3 million dollars. The problem presented by these trends is of general concern to railway management.[93]

It was for such reasons that the District Court, with its special opportunities for knowledge of the property, found that the "very large" increase in basic costs "more than offsets the economies effected by the Improvement Program." (R. 218-19) The burden of this increase can be expected to show in unmistakeable terms as the extraordinary volume of war time traffic recedes to a peace economy with the restored and intensified competition it will inevitably bring. A solemn warning is supplied by the Commission's finding in *Missouri Pacific Reorganization*, 257 I. C. C. 479, 526-7

[92] Railway Operating Revenues include all receipts from transportation. Deducting railway operating expenses, income and other taxes and the net payments for car hire and joint facilities produces net railway operating income. Adding income from non-railroad sources produces Gross Income.

[93] See J. J. Pelley, President, Association of American Railroads, quoted in The New York Times, December 27, 1945, p. 25, column 6; R. E. Woodruff, President, Erie Railroad Company, *id.*, January 2, 1946, p. 25, column 2.

(1944) that if the Missouri Pacific income account in 1940 were recomputed on the basis of 1944 unit costs, its 13 million dollars reported net available for interest in 1940 would be changed to a deficit of 11 million dollars. It was natural, therefore, for the Circuit Court to say:

> "It is not unreasonable to assume that if these improvements had not been made, the probable earning capacity would have been substantially reduced." (R. 244)

Rates.—The downward trend of rates on the Rio Grande has been pointed out, but its effect on net earnings is too vital to go unmentioned here. The Rio Grande's greatest net earnings available for interest before the extraordinary war years were in 1926 and 1929. Yet the net earnings available for interest reported in those years, taken together, would have been almost wholly extinguished if the 1944 levels of rates had prevailed at that time.[34]

Liberality of Commission.—These were matters to be weighed by the Commission and it was entitled in their light to find that there is no prospect of a future more brilliant than will accommodate the Plan. The inadequacy of 1921-1944 earnings to cover dividends on the new Common Stock is, especially in the light of the current trends noted above, in itself sufficient evidence to support the Commission's conclusions. Indeed they indicate that the Commission has been liberal, and so it has, more so than its custom in other cases. It may be noticed from the published reports of the Commission that the new capitalization in this case is larger than the average of all other important railroad cases, whether viewed in relation to the largest earnings in any year of the decade 1930-1939 or in relation to the physical

[34] The sum of the net earnings available for interest in 1926 and 1929 would have been reduced from 16.5 million dollars as reported to 1.1 million dollars. See Annual Reports.

values found by the Commission. Moreover, past earnings in this case were appraised not only in the light of a 5% capitalization rate, or 20 times earnings, the Commission's most usual test,[29] but also of a 4% rate, or 25 times earnings. No railroad reorganization under Section 77 has used a more liberal test. It is much more liberal than the Securities and Exchange Commission practice for the more stable electric utility industry.[30] The District Court was troubled on this score, saying

> ". . . it is very doubtful to my mind if the new capital structure is not too large" (R. 1065).

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[29] *E. g.*:

Chicago Great Western R. Co. Reorganization, 228 I. C. C. 585, 611-12 (1938), 233 I.C.C. 63 (1939); approved *In Re Chicago Great Western R. Co.*, 29 F. S. 149, 160 (N. D. Ill. 1939);

Akron, Canton & Youngstown R. Co. and Northern Ohio R. Co. Reorganization, 228 I. C. C. 645 (1938), approval affirmed *Akron, Canton & Youngstown R. Co.* v. *Hagenbuch*, 128 F. 2d 932, 937-8 (C. C. A. 6, 1942), *cert. den.* 318 U. S. 794 (1943);

Chicago and North Western R. Co. Reorganization, 236 I. C. C. 575, 628 (1939), 239 I. C. C. 613 (1940), approved *In Re Chicago and North Western R. Co.*, 35 F. S. 230 (N. D. Ill., 1940), *aff.* 126 F. 2d 351 (C. C. A. 7, 1942), *cert. den.* 318 U. S. 793 (1943);

New York, New Haven and Hartford R. Co. Reorganization, 239 I. C. C. 37, 97-8 (1940), 244 I. C. C. 239 (1941), 254 I. C. C. 63 (1942); 254 I. C. C. 405 (1943), 257 I. C. C. 9 (1944), approved *In re New York, New Haven and Hartford R.*, 54 F. S. 595, 601 (D. Conn. 1943), 54 F. S. 631 (D. Conn. 1944), *aff.* 147 F. 2d 40 (C. C. A. 2, 1945), *cert. den.* —— U. S. ——, 89 L. ed. 1553 (1945);

Erie R. Co. Reorganization, 239 I. C. C. 653, 716-17 (1940), 240 I. C. C. 469 (1940), approved *In Re Erie R. Co.*, 37 F. S. 237 (N. D. Ohio 1940).

[30] *Portland Electric Power Co.*, S.E.C. Holding Company Act Release No. 6365, Jan. 15, 1946, at p. 17 (8 1/3%); *York Railways Co.*, Release No. 6285, Dec. 11, 1945, at p. 17 (5.6%); *International Utilities Corporation*, Release Nos. 4896, Feb. 15, 1944, and 4992, April 14, 1944 (8%); *Stanley Clarke*, Release No. 4985, April 15, 1944 (8-11%); *Columbia Gas and Electric Corporation*, Release No.

Similarly Trustee Swan, in the greatest earnings year of all history, testified:

> "Our problem is: what will the Trustees do to make possible an earning capacity to justify the Interstate Commerce Commission Plan? This is a fact. This is no theory." (R. 1006)

Circuit Court's Action.—This is the record on which the Circuit Court requires the Commission as a matter of law to *increase* the capitalization provided for in the Plan. It does this by directing that "all excess war profits yet to accrue" shall go to the General Mortgage Bonds (R. 247, 248, 249) and that for all later time any "greater net returns than anticipated in the plan" shall go to the General Mortgage Bonds (R. 250). Any such right of participation in future earnings is a security, and the particular legal form that may be chosen to evidence it is a matter of no consequence. The Circuit Court recognized this by suggesting for the Generals an additional issue of "a subordinate stock which would receive returns only from excess dividends" (R. 250), subordinate, that is, to the new Common Stock. The Circuit Court admitted that the particular method of arranging this participation was for the Commission to determine, but since no securities can possibly be taken from the Senior Creditors, an increase in total new capitalization is the inevitable consequence of the decision if it should stand.

It is remarkable, we think proper to say, that an appellate court, rightly declaring that the Commission's action "in

3885, Nov. 10, 1942 (8%); *Derby Gas and Electric Corporation*, Release No. 2985, Sept. 6, 1941 (about 7%); *Mountain States Power Co.*, 5 S. E. C. 1, 7 (1939) ("7% or even 6%"); *Northern Indiana Public Service Co.*, 5 S. E. C. 239 (1939) (6%); *Utilities Power and Light Corp.*, 5 S. E. C. 483 (1939) (5.25% on a consolidated basis). See also *Massachusetts Utilities Associates*, 5 S. E. C. 88 (1939) (gas; 5%), and *Peoples Light and Power Co.*, 5 S. E. C. 461 (1939) (gas; 6 2/3%, 7% and 8%).

fixing the valuation and setting up the capital structure is free from . . . infirmities, and . . . must be upheld" (R. 245), should immediately require an important increase in that capital structure. The remarkable nature of this action is not diminished by the fact that it is the first time any court has overridden the Commission's judgment on the total amount of the permissible new capitalization, or by the fact that the stage for this innovation is a case where historical earnings have been seriously inadequate to provide a fair return on the new securities already called for in the Commission's Plan.

The Circuit Court's action should be reconciled with its declaration by reversal. As this Court said:

> "So long as legal standards are followed, the judgment of the Commission on such capitalization is final." (*Western Pacific Case*, 318 U. S. at 474)

> "The basic question in a valuation for reorganization purposes is how much the enterprise in all probability can earn . . . Certainly there is no constitutional reason why earning power may not be utilized as the criterion for determining value for reorganization purposes. And it is our view that Congress when it passed §77 made earning power the primary criterion." (*Milwaukee Case*, 318 U. S. at 540-41)

War Earnings.—The only imaginable basis for a view that there was no evidence to support the Commission's action, or that it applied an erroneous standard, would be that the peak earnings of war-time must be accepted as the norm for the future. But the Circuit Court itself disclaimed such an approach, saying that

> "These earnings are to a great extent artificial, and will disappear largely with the coming of the peace. They have very little value in estimating the probable future earnings of this property in the peace economy

which is to come. The Commission was well within its right in largely disregarding them . . ." (R. 242)

This was also the express view of the Commission[97] and the District Court[98] and is in accord with this Court's admonition that

". . . the bulge of war earnings *per se* is unreliable for use as a norm unless history is to be ignored . . ." (*Milwaukee Case*, 318 U. S. at 543)[99]

The record here precludes the possibility of any different view.

So it is immaterial that war-time earnings have been so high as to make up for regular failure of the road to earn interest on the Senior Debt in all the years of the reorganization proceedings before 1942, and indeed to leave a substantial amount of reported earnings for the whole elapsed period of the proceeding in excess of interest on the Senior Debt (R. 349). That merely dramatizes the spectacular extent of the non-recurring and non-capitalizable war-time earnings. Nor can the General Mortgage Trustee assert any special claim to additional new securities on this account

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[97]R. 158-9, quoted at p. 20 above. The Commission has repeatedly expressed similar views in other cases; see *Chicago, Rock Island & Pacific R. Co. Reorganization*, 257 I.C.C. 265, 286 (1944), *St. Louis-San Francisco R. Co. Reorganization*, 257 I.C.C. 399, 409 (1944); *Missouri Pacific Reorganization*, 257 I.C.C. 479, 522-27 (1944).

[98]R. 192, 194, quoted at p. 22 above, and R. 219-20, summarized at p. 24 above.

[99]The same view has been repeatedly taken here and in the lower courts; see:

Western Pacific Case, 318 U. S. at 508-9 (1943);
I. C. C. v. Jersey City, 322 U. S. 503 (1944);
In re New York, New Haven & Hartford R., 147 F. 2d 40, 45-6 (C. C. A. 2, 1945), *cert. den.* —— U. S. ——, 89 L. ed. 1553 (1945);
In re Chicago, Milwaukee, St. Paul & Pacific R., 145 F. 2d 299, 303 (C. C. A. 7, 1944).

because of any view of a lien on impounded income. All income was subject to the prior liens of the Senior Debt both by seasonable sequestration petitions and by mere possession of the Debtor Trustees,[1] and 77 million dollars of principal of Senior Debt had matured in addition to the 16 million of interest to January 1, 1943, a sum approximating twice the total net available for interest on funded debt reported since the inception of the proceeding.

These considerations, we submit, require that the Circuit Court should be reversed in so far as it requires changes in the Plan because of future earnings, in order that, in this respect also, the orders establishing the Plan may be affirmed.

Peril to Public Interest.—This is not a case where adherence to established procedure is important only to avoid the possibility of evils in other cases, for the Circuit Court's action directly obstructs the public interest in the capitalization of this property.

The purpose of the Congress in the enactment of Section 77 was to remove, rather than perpetuate, the causes of bankruptcy.[2] It is well known that unsound financing through persistent increase in debt has been a major cause of the chronic financial difficulties of the railroads, and that the only alternative, where new money is needed, is sale of stock.[3] This is possible only where the quantity of stock is so limited in relation to earnings as to give it an investment quality. Such limitation, and the preservation of a genuine possibility of equity financing, are thus matters that "affect

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[1] *Central Hanover Bank and Trust Co. v. Philadelphia & Reading Coal & Iron Co.*, 99 F. 2d 642, 645 (C.C.A. 3, 1938); *In Re Philadelphia & Reading Coal & Iron Co.*, 117 F. 2d 976, 978 (C. C. A. 3 1941).

[2] H. R. Rep. No. 1336, 74th Cong., 1st Sess. (1935) 6.

[3] Commissioner Eastman dissenting in *Chicago, Milwaukee and St. Paul Reorganization*, 131 I. C. C. 673, 701 (1928).

the public interest immediately and directly.'" The Commission was alive to the realization of both those purposes in this case and acted "so as to facilitate the use of stock in future financing." (R. 69)

The illusory sub-common stock that the Circuit Court conceives beyond the visible reach of earnings could have no investment attributes. It would be a mere speculative token, and its very existence, draining off the earnings of prosperous years, would degrade the new Common, for in that state of affairs the new Common could never recoup the losses of bad years from the "excess" earnings of prosperous years. Thus the new Common would in effect become a second preferred stock; at a point in earnings that would give it deceptive potentialities in the market. This limitation of return might also have serious consequences on the incentive to effective corporate management.

The problem of voting power for the new sub-common stock carries an equal menace. If it has no vote, it will be scandalous; if it has a vote, it will displace, in some degree, effective control from the area of effective ownership, with the evils that notoriously follow.

So in multiple respects exact obedience to the Circuit Court would disrupt sound financial practice. Approximate obedience to the Circuit Court through the means of an enlarged issue of the new Common itself would also involve many of these same disadvantages. As the Commission recently said:

> "If the amount of junior securities of a company is far in excess of its expectable earning power, additional securities of that character must be sold, if sold at all, at prices which are prohibitive, taking into consideration the amount of cash which would have to be raised and the plant additions to be financed. Reorganizations

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'*Western Pacific Case*, 318 U. S. at 474.

should remove rather than perpetuate the cause of bankruptcy, and should not be a means of misleading old and new investors. That desired effect can result only if the new securities are so related in character and total amount to the ability of the reorganized company to pay interest and dividends, that such securities possess an actual value and not merely one that is speculative." (*Missouri Pacific Reorganization*, 257 I. C. C. 479, 524 (1944))

The public interest sought to be safeguarded by the limitations on appellate action, is thus directly in peril from the action of the Circuit Court.

2. The Circuit Court Defeats the Private Right to Full Satfaction.

(a) Introduction

Here we invoke the private right of the Senior Creditors to be made whole before the General Mortgage Bonds can have any substantial participation, a right which the Circuit Court's decision will defeat.

This private right is invoked not only for its immediate importance to the Petitioners, but also for its consequential importance to the railroad industry and the public. Through all history the railroads have obtained substantial parts of their necessary capital in the form of senior debt, where capital is supplied for a fixed return, without hope of incremental profit, relying on the right to be made whole in an actual and realistic sense before any provision for junior interests. To protect the availability of such credit on cheap terms for the future it is important that the agreed protection be supplied in actual practice as well as by abstract pronouncement.

(b) The Absolute Priority Rule

Prior to the corporate reorganization acts the repeated pronouncements of this Court that stockholders can have

nothing "until all the debts of the corporation are paid"[5] were translated in many reorganizations into a doctrine of relative priority. This said that, so long as the relative positions of the respective classes of old claims were substantially maintained, either in stratified form through a qualitative recognition of priorities in different grades of new securities (which the Circuit Court attempts here by its new sub-common stock) or in commuted form through a quantitative recognition of priorities in different amounts of the same grade of new security, all classes of old claims might be recognized, without regard, or largely without regard, to the value of the realization so provided. This doctrine made possible the continuation of all the old classes even though the senior ones were not made whole, and led to the creation of excessive new capitalizations.[6] On the other hand there were those who, mindful that the creditor's contract is one to be paid,[7] and not merely to be better off than someone else, believed that it was not enough to give him for his old debt new securities of an equal face amount regardless of their value, but each creditor, in his order of rank, must receive new securities having a fair value approximately equal to his total claim before any junior claimant might be recognized. This was the doctrine of absolute priority.

The asserted doctrine of relative priority, on which the Circuit Court seemingly rests here, has now been rejected in categorical terms by this Court and the doctrine of ab-

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[5] *Chicago, Rock Island and Pacific R.* v. *Howard*, 7 Wall. 392, 410 (U. S. 1868); *Louisville Trust Co.* v. *Louisville, New Albany & Chicago R.*, 174 U. S. 674 (1899); *Northern Pacific R.* v. *Boyd*, 228 U. S. 482 (1913).

[6] Moulton and Associates, *The American Transportation Problem*, (1933) pp. 349-52.

[7] This right, and the related interests of the security position, are constitutionally protected: *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555 (1935); *Wright* v. *Vinton Branch*, 300 U. S. 440 (1937).

solute priority established. In *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106 (1939), the Court, in accordance with the arguments of the Interstate Commerce Commission and the Securities and Exchange Commission that contracts have "an unreal quality" unless the creditor receives "recognition approximating full payment",[8] held that creditors are "entitled to be paid" and not merely to retain a superior position irrespective of actual realization (pp. 119-20).

This was made even clearer in *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510 (1941). There the plan gave the bondholders new securities of a face amount equal to the whole of their principal (half in income bonds and half in preferred stock), but made no provision for their unpaid interest, and at the same time recognized the old stock (the old preferred in new common and the old common in warrants). There was no adequate determination in the trial court of reorganization value.[9] The Court held that the confirmation of the plan was erroneous. "The full and absolute priority rule" of the *Boyd Case* and the *Los Angeles Case*, it held, precludes any participation by equity interests "until the bondholders had been made whole" (520-1). They could not be properly taken as "made whole" in that case because they received nothing for their unpaid interest and, quite apart from that, for two additional reasons:

(a) There was no adequate finding of value, and such a finding, in terms of prospective earnings, is essential to a determination of fairness:

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[8] Brief in that case for the United States, *amicus curiae*, at pp. 17 and 25.

[9] For the whole property, with which we are here concerned, or of the component parcels; a matter of no interest here. Since the Company was an industrial, no commission action was required.

"Whether or not the earnings may reasonably be expected to meet the interest and dividend requirements of the new securities is a *sine qua non* to a determination of the integrity and practicability of the new capital structure. It is also essential for satisfaction of the absolute priority rule of *Case* v. *Los Angeles Lumber Products Co.*, *supra*. Unless meticulous regard for earning capacity be had, indefensible participation of junior interests in plans of reorganization may result." (525-6)

(b) The bondholders were not compensated for their surrender of senior rights in receiving the new junior securities:

"True, the relative priorities are maintained. But the bondholders have not been made whole. They have received an inferior grade of securities, inferior in the sense that the interest rate has been reduced, a contingent return has been substituted for a fixed one, the maturities have been in part extended and in part eliminated by the substitution of preferred stock, and their former strategic position has been weakened. Those lost rights are of value. Full compensatory provision must be made for the entire bundle of rights which the creditors surrendered." (527-8)

". . . while creditors may be given inferior grades of securities, their 'superior rights' must be recognized. Clearly, those prior rights are not recognized, in cases where stockholders are participating in the plan, if creditors are given only a face amount of inferior securities equal to the face amount of their claims. They must receive, in addition, compensation for the senior rights which they are to surrender. If they receive less than that full compensatory treatment, some of their property rights will be appropriated for the benefit of stockholders without compensation. That is not permissible." (528-9)

The test to govern these questions of compensation was made clear in these words:

> ". . . whether in case of a solvent company the creditors should be made whole for the change in or loss of their seniority by an increased participation in assets, in earnings or in control, or in any combination, thereof, will be dependent on the facts and requirements of each case. So long as the new securities offered are of a *value* equal to the creditors' claims, the appropriateness of the formula employed rests in the informed discretion of the court." (529-30, italics added.)

In other words, any set of new rights will be adequate compensation for the old if of "a value equal to the creditors' claims," but no set of new rights can be unless it is of that value.

This holding, we submit, clearly settles the law. It was supplemented in the two railroad cases, which are the latest important decisions in this field.

In the *Western Pacific Case*, the Court expounded the absolute priority rule as requiring that:

> "senior claims first receive securities of a worth sufficient to cover their face and interest before junior claims receive anything." (318 U. S. at 483).

This is a holding in terms that the absolute priority rule theretofore laid down as between creditors and stockholders applies equally as between senior and junior classes of creditors, the exact situation presented in the case at bar. Similarly it was held in the *Milwaukee Case:*

> "The rule of the *Boyd* case 'protects the rights of senior creditors against dilution either by junior creditors or by equity interests.' *Marine Harbor Properties* v. *Manufacturers Trust Co.*, [317 U. S. 78, 87]" (318 U. S. at 569).

On the standard of value, the Court in the *Milwaukee Case* said:

> "Only 'meticulous regard for earning capacity' . . . can afford the old security holders protection against a dilution of their priorities and can give the new company some safeguards against the scourge of overcapitalization." (541)

As applied to the question whether the old stock may be recognized, that standard puts the question:

> "whether there is a reasonable probability that the earning power of the road will be sufficient to pay prior claims of interest and principal and leave some surplus for the service of the stock." (541)

On the question of compensation for surrender of senior rights the Court in the *Milwaukee Case* reaffirmed the rule in the *Rock Products Case*, pointing out that:

> "Unless that principle is respected, there will be serious invasions of the rights of senior claimants to the benefit of junior interests. The property of one group will be subtly appropriated to pay the claims of another while lip service is rendered the principles of priority." (570)

It is, therefore, settled that senior creditors must be made whole by receiving new securities with a value approximating their total claim before any junior interest may be recognized.

(c) The Test of Value

"Value" is, of course, a word of many meanings (*Milwaukee Case* at 540), but the use here of that term, or of the Court's other term "worth", does not raise any new problems or any further obscurity. It is clearly designed

to mean something that makes the creditor "whole" by giving him "completely compensatory" treatment in a sense that a practical man of affairs can understand. That necessarily means new securities approximately equivalent to a payment in cash.

There is room for a good deal of elasticity in the time as of which that "value" is determined. The most rigid view would be spot market value at the time of issuance.[10] But this would permanently rearrange ownership on the basis of conditions that chanced to exist at a particular moment, even though those conditions might reasonably be judged temporary, and thus impose undue sacrifices, which were not the purpose of the Act.[11] The equitable rule implicit in the decisions of this Court, we submit, is that reorganization value is to be determined on the basis of the earning power that appears to be the reasonably assured expectancy. The Court's test of "reasonable probability" quoted above from the *Milwaukee Case* is an illustration, and further in point as emphasizing that the value of the distributed securities, and not the value of the assets, is the controlling criterion. If the creditor can not realize that value now, but only later, the rule itself requires a high degree of real assurance.

The creditor may not complain that he has to wait if the period of waiting is not so long as to endanger ultimate satisfaction in full. Nor may the junior interest complain if the creditor is merely getting his agreed treatment. But the creditor is entitled to complain if he is put in risk of loss by postulations of an indefinite future. And the junior interest is not entitled to protection at the cost of shifting the risk of loss from himself to his senior.

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[10] This view has, indeed, been expressed: Dean, *A Review of the Law of Corporate Reorganizations* (1941) 26 Cornell L. Q. 537, 559, n. 63.

[11] S. Rep. No. 1336, 74th Cong., 1st Sess. (1935) 3.

This "reasonable probability", therefore, does not look to spot market at moment of issuance, but it must look to conditions of which the evidence provides reasonable assurance within the reliable future. We do not seek a nice precision of equivalence, for in judgments of future probabilities "'an estimate, as distinguished from mathematical certitude, is all that can be made'" (*Milwaukee Case* at 542). Nor do we contemplate the delusive exactitude of detailed findings of future markets, for that would only afford "an apparent certainty . . . which does not exist in fact." (*Milwaukee Case* at 562) But lest the absolute priority doctrine evaporate into metaphysics, it is essential that its touchstone remain as realizable value, not a mere balancing of investment attributes in the abstract, but an appraisal of them in the light of what people will probably pay. As the Circuit Court of Appeals for the Second Circuit said:

> "Value depends on what people will pay . . ." (*In re New York, New Haven & Hartford R.*, 147 F. 2d 40, 48 (1945) *cert. den.* —— U. S. ——, 65 S. Ct. 1577, 1578 (1945))

It is only when people will probably pay the full amount at which the new securities are used to satisfy existing debts that creditors are "made whole" in the realistic sense intended by this Court, and only when this probability looks to a time reasonably close to the date of exchange and not to the clouds of the distant, and thus conjectural, future.

(d) These Principles Are Violated by the Circuit Court

The Commission found that "the value of the combined properties for the purposes of this proceeding is approximately $155,173,127" (R. 159). But this was apparently

done with a considerable view to "maximum limits".[12] It does not seem that the Commission had any expectation of a market value for each class of the new securities approximating their face amount at any reasonably near date. Indeed, there are indications to the contrary. Its finding on total capitalization was only that it "should not exceed approximately that amount" (R. 159). And it held that RFC, with its award of new First Mortgage Bonds and new Income Bonds for the full amount of its claim, was "not fully secured" and was thus entitled to realize also on its rental claim (R. 178). With respect to the stock to be issued by the reorganized company it said in its first report that the new debt should be so limited "as to render the payment of dividends probable, at least on the new preferred stock, under normal conditions of business" (R. 68). This implies that the Common must look to periods of exceptional railroad prosperity for its return, the very periods, it will be noted, when the Circuit Court channels off all "excess" earnings for the General Mortgage Bonds. The meaning is only that the new Common has "some prospect" of value.[13]

So the Commission did not, we believe, make any finding that the new Common Stock was the equivalent of money in its face amount, presently or at any assured future time. Rather it based its finding of adequate compensation to the Senior Claims on the particular provisions of the Plan, saying that:

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[12] *Opening Journal Entries for Reorganization of Chicago Great Western R. Co.*, 247 I.C.C. 193, 195-6 (1941), reannounced as of general application in *Missouri Pacific Reorganization*, 257 I. C. C. 479, 522 (1944).

[13] Thus *Chicago, Indianapolis & Louisville R. Co. Reorganization*, 254 I.C.C. 539, 565 (1943) and *Alabama, Tennessee & Northern R. Corp. Reorganization*, 247 I.C.C. 453, 465 (1941). Since prospects are always reflected in the market, this contemplates some actual present value (*Missouri Pacific Reorganization*, p. 69 above), though considerably less than par (*Chicago, Rock Island & Pacific R. Co. Reorganization*, 257 I.C.C. 265, 278 (1944)).

"the compensation to the . . . [Senior Creditors] would be adequate under the provisions of the plan . . ." (R. 169)

From the point of view of the new Common Stock, the pertinent "provisions of the plan" are that the new Common Stock represents all that may be left of reorganization value and all of it except 10% is given to the Senior Creditors. This participation for the Generals is not large enough to raise any important issue and no objection to it is presented in these appeals.

There can be no doubt that the District Court followed similar reasoning, for its view of the Common Stock was a somber one. Indeed it said, as shown above, that the new Common "has little or no value" (R. 220), and, if any, then wholly because of the improvement work and the increase in current assets (R. 222).

The Circuit Court breaks down each of these justifications for the Plan. It changes the capitalization so that the new Common provided for in the Plan no longer represents the whole residual equity. Then it diverts the newly required additional securities from the Senior Creditors to the Generals. Thus it takes from the Senior Creditors the present value of a chance to be made whole out of the high earnings of prosperous years in the future, as it has already taken from them the present value of the cash on hand.

This invasion of the Commission's function to determine values[11] can not be justified under a fiction that only a pure question of law is involved (R. 253). Prospective earning capacity is as straight an issue of fact as present cash requirements. Nor can it be justified on the view that exceptionally prosperous years were omitted from the Commission's consideration. It was the Commission's duty, in concluding that the new Common had some prospect of value, to consider the likely results in extraordinarily good years

[11] *Western Pacific Case*, 318 U. S. at 473.

as well as those in extraordinarily bad years, for the long future includes both. That it did so is in terms found by the Circuit Court (R. 242) and it is plain from the Commission's reports that it is precisely the earnings of extraordinarily good years that alone give any prospect of value to the new Common.

So the decision is a frontal attack on the Commission's powers, and a substitution of the Court's own judgment on the amount of the new capitalization. This is made in a case where there was evidence to support the Commission's conclusions. The earnings record, as we have pointed out, shows nothing available for the new Common already provided for in the Plan except in the extraordinary conditions of war-time, which are admitted in the Court's own opinion to be both temporary and non-recurring (R. 242). No heed is given to the relentless march of operating costs, which the District Court found were of such extent as "more than offsets the economies effected by the Improvement Program" (R. 218-19), and which the Circuit Court itself observed to leave less net earnings from greater total operating revenues in 1943 than in 1942 (R. 244). There is no reference to the impact of such new costs on the lower total operating revenues of peace-time that the Circuit Court itself expects. The Commission's finding which the Circuit Court sets aside in the face of this evidence is fundamental to the validity of the Plan. The result is to take from the new Common of the Senior Creditors its only hope of value by diverting to the General Mortgage Bonds the exclusive claim, or an enhanced share, in the high earnings of prosperous years.

This, we submit, erodes all meaning from the "full and absolute priority rule" laid down by this Court. Without pretense of any finding that Senior Creditors will really and actually be made whole, the Circuit Court appropriates the property of one group to pay the claims of another.

There can be no logical explanation of such action except

a theory that otherwise the Senior Creditors would receive more than the amount of their claims. This is contrary to the findings of the Commission and the District Court and there is no evidence to support such a view. Indeed that they can not in fact receive more than their claims is clear on any realistic analysis of earning prospects.

On that point the quotations on the when-issued market are an illuminating supplement. The new securities provided for in the Plan are regularly sold over the counter on a when-issued basis and quotations are regularly reported in the standard financial journals. It is proper to take judicial notice of them.[15] We do not, of course, refer to them as conclusive proof of value, nor do we invoke any theory of spot market value as a test of satisfaction. But as independent, though inconclusive, judgments, they are useful for general indications. They appraise the new Preferred between a half and two-thirds of its par amount, and the new Common between a quarter and a third of its par amount.[16] Even at the highest prices, the Senior Creditors who receive any of the new Common will, on the average, realize, from all their new securities, less than two-thirds of their total

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[15]Thus, in *Wallace* v. *Franz*, 68 F. 2d 313 (C.C.A. 8, 1933) the court took judicial notice of market quotations after the closing of the record below. More recently it has been said in railway reorganizations:

> "We may take judicial notice of the fact that neither stock has substantial market value and has not for five years" (*In re Chicago, Milwaukee, St. Paul & Pacific R.*, 124 F. 2d 754, 762, n. 1 (C. C. A. 7, 1942) *aff.* in *Milwaukee Case*, 318 U. S. 523 (1943)).

> "We must take judicial notice of the fact that most of them [the bonds], during the last five years have sold at around 10¢ on the dollar. Not one of them has sold at or near par" (*In re Chicago and North Western R.*, 126 F. 2d 351, 367 (C. C. A. 7, 1942) *cert. den.* 318 U. S. 793 (1943)).

[16]The exact figures are shown in Appendix G, both for market prices of the new securities and for resulting realization on the present securities.

claim, and one of them will receive only about half its total claim.

This is generally typical of the reorganizations that have been completed, for with only one exception, as the following table shows, the new Preferred and Common stocks have not sold as high as the par or stated amounts at which they were distributed in the respective plans:

	Preferred		Common	
Road	*Par or Stated Amount*	*Highest Market in 1945*	*Par or Stated Amount*	*Highest Market in 1945*
C&EI	$ 40	$26	$ 51.09	$12⅝
CGW	50	34¼	50.00	12½
CMSt.P&P	100	74	100.00	33
C&NW	100	76⅞	100.00	49½
Erie	100	86	40.00	20½
W. P	100	92	57.00 and 62.00	57⅛

There is, accordingly, no basis for any thought that the Senior Creditors will be overpaid. The action of the Circuit Court in requiring additional securities for the General Mortgage Bonds representing an enhanced share in future earnings subverts the "full and absolute priority rule" and should be reversed so that, in that respect also, the orders establishing the Plan may be affirmed.

III
EQUIPMENT TRUST OBLIGATIONS AND JUNCTION BONDS

(a) Introduction

Since the stated effective date of the Plan and the Commission's approval of it, two issues of senior debt have been paid or acquired, in whole or in part, by the Debtor Trustees. Thus cash that would otherwise remain among the assets of the estate has been disbursed and the initial debt capitalization under the Plan has been reduced by an equal amount, leaving net worth unchanged. In both instances the Circuit Court held that an equal face amount of additional new securities must be issued, contrary to the plain terms of the Plan. For brevity, both questions may be discussed together.

(b) The Facts

The facts are that on January 1, 1943, the stated effective date of the Plan, $5,758,000 aggregate principal amount of equipment trust obligations were outstanding, all issued by the Debtor Trustees.[17] These matured serially in the aggregate principal amount of $609,000 a year.[18] The Debtor Trustees met these maturities when due. So $1,218,000 principal amount were paid in the two years 1943-44.

The Plan provides that:

> "The capitalization of the new company, as of January 1, 1943, after consummation of the plan . . . shall consist substantially of the following securities . . . the amounts stated being subject to reduction to the extent, if any, that matured interest proposed to be funded in

[17] R. 182, Annual Report 1943, pp. 13 and 15.

[18] 1 Tr. 5018 (1942 Ct. Ex. 7).

the plan is paid, and as equipment obligations or other liabilities are paid or reduced . . ." (R. 2-3)

The other debt in question was the Rio Grande Junction Bonds, with a total claim for principal and interest to January 1, 1943, of $2,758,333 (R. 183), secured by a first lien on 62 miles of the main line in Colorado that are owned by a subsidiary and leased to the Rio Grande (R. 38). As stated at p. 22 above, a contention had been made in the proceedings before the Commission that these bonds were not subject to modification in bankruptcy because the Junction Company was not a party to proceedings under Section 77. To avoid any delay on this account in the consummation of the rest of the Plan, the Commission provided that the District Court might exclude the Junction Company from the Plan and consummate the rest of the Plan independently.[19] The controversies arising on this point before the District Court at the hearing on approval of the Plan made it evident that delay might well ensue unless it should avail of this permission. So it did. Expressly relying on this provision of the Plan and the further provision by which the District Court was empowered to construe the Plan and cure defects, the District Court caused the Debtor Trustees to purchase the Junction Bonds at their principal plus interest accrued at their coupon rate (R. 199-201). Recognizing that the Junction Company was excluded from the Plan by this action, the Commission did not submit the Plan to the Junction bondholders (R. 28). In result the reorganized company will receive all securities of the Junction Company and will thus be in a position to take over its assets.

In both instances the Circuit Court held that the "new securities set apart for the payment" of the old debt[20] would

[19] R. 166 and 2.

[20] "New securities" were in fact provided only for the Junction Bonds. The equipment trusts were to be assumed.

not be needed and, since the Senior Claims "had been paid in full";

> "... this undistributed value [in respect of the Junction Bonds] in all equity and fairness belongs to the General Bondholders. Any plan which does not give it to them does not comply with the requirements of Section 77(e) of the Act." (R. 251)

> "This unused value [as to the equipment trusts] belongs to the General Bondholders." (R. 251)

By the previous discussion in this brief we have shown that the Plan, apart from these two points, was within the powers of the Commission and the District Court and is thus conclusive in the Circuit Court. On that premise we now inquire whether the Circuit Court had the power to require modifications of the Plan because of these two points. We submit that it did not and that its action is illegal for two reasons: (*i*) as usurping the Commission's power to fix the new capitalization in the public interest and (*ii*) as usurping the Commission's power to provide full satisfaction for private rights.[21]

(c) The Public Interest

The Plan provides for much more initial debt than the Commission had previously thought permissible, indeed 11 million dollars more.[22] The improvements that had been made were an aid to this action (R. 118-119), but so was present and prospective cash, for it was expected, apart from covering the needs of operation and providing a fair return on the new securities, to flow into further

[21] No question arises here whether the Junction bondholders received too much by the purchase, for that question could have been presented only in appeal from the order directing the purchase, and none was taken.

[22] *Cf.* R. 184 and R. 352.

improvements.[23] It was, in other words, the whole bundle of assets to which the Commission looked in finding reorganization value. So if cash should be paid out on old debt dealt with in the Plan, it was understandable that the Commission might require the new debt to be correspondingly reduced. It knew, of course, that such payments would be made on equipment trusts, for they were all issued by the Debtor Trustees, with serial maturities that were being regularly met. Conceivably, also, similar payments might be made on other debt dealt with in the Plan. So the Commission provided in the Plan that any reduction of "equipment obligations or other liabilities" should reduce, by an equal amount, the new capitalization (R. 2-3).

The contingencies so provided for having occurred, the new capitalization under the Plan is the amount fixed by the new state of affairs and thus excludes provision for the paid equipment trusts and the purchased Junction Bonds. As to the equipment trust obligations, no new securities were ever provided for them, but there was merely to be an assumption of those at the time outstanding. There being a smaller amount, the only consequence is that the smaller amount alone is to be assumed. Similarly on the Junction Bonds, the provisions for the Junction Company having been excluded from the Plan, there are no provisions in the Plan for an issuance of new securities in that respect. The situation is merely that the Debtor Trustees have invested a part of their funds, choosing, in lieu of additions and betterments, for example, the bonds of the Junction Company.

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[23] Thus see R. 155-158. The evidence indicated that from the cash on hand at January 1, 1943, or thereafter received, about 14 million dollars was to be used to pay for improvements to the property (R. 1021-22, 1186). A further improvement program was also expected (R. 1028).

Under the general rule of administrative action (p. 57 above), it is the result that matters, and not the intermediate steps by which it is reached. The question is whether it was within the power of the Commission to limit new capitalization to the amount presently and effectively provided for in the Plan. That question is controlled, of course, by the earnings prospects. They have been discussed above. All that discussion has omitted, from the requirements to service the new securities provided for in the Plan, all equipment trust obligations and all the new securities originally provided for the Junction Bonds. Even so, historical earnings have been inadequate, except in the war years, to provide a fair return on the remaining new securities that will be actually issued, and mounting levels of costs put problems for the future. Plainly, therefore, there was evidence to support the Commission's action. This is decisive. Yet the Circuit Court, overriding the express limitation in the Plan, requires the issuance of additional new securities in lieu of those paid or purchased, though the cash so used is no longer there and the equipment has depreciated. To issue the original debt on reduced assets is to increase capitalization as surely as to issue greater debt on the original assets. Both dilute the ratio of security. Such action is, accordingly, beyond the Circuit Court's appellate jurisdiction.

Some considerable latitude of discretion must, as a practical matter, be allowed the Commission in these decisions. For one thing, there is no formula to produce precise answers in such areas of judgment. Indeed any such approach would only "create an illusion of certainty where none exists" (*Milwaukee Case*, 565). But what is more, the railroads do a continuous job and every day brings some degree of change. As an illustration, we suggest that the Debtor Trustees are now engaged in issuing $2,610,000 of new equipment

trust certificates, a sum twice as large as the reduction considered by the Circuit Court.[4] Other changes will no doubt occur. The concepts of the law must not be drawn too fine for the accomplishment of the practical task. If any substantial change were allowed to invalidate a plan, it might well prove impossible to complete the reorganization of any railroad. As the Court has said, interpretations that would place "an impracticable burden on the whole reorganization process" (*Milwaukee Case* at 565) are to be avoided.

(d) Private Right

It may well be that the words of the Circuit Court intend that the General Mortgage Bonds shall receive new bonds equal to those originally provided for the Junction Bonds and equal to the amount of the equipment trusts that have been paid. If so, that is another glaring defiance of the priority rule, comparable, though somewhat less extreme, to its award to them of cash discussed at p. 53 above, for the Plan requires the Senior Creditors to take new Common Stock for a substantial part of their total claim. But even if the words of the Circuit Court contemplate some increase in the allotment of new bonds to the Senior Creditors, and a transfer of an equal face amount of new Common Stock to the Generals, that also, we submit, is a violation of the right of the Senior Creditors to full satisfaction of their claims.

The Plan being validly established by the concurring action of the Commission and the District Court, all junior security holders cease to have any interest in the property except, in the case of the General Mortgage Bonds, the limited participation allotted them in the Plan. Thereafter it

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[4] *Denver and Rio Grande Western Railroad Company Trustees Equipment Certificates*, F. D. No. 15,046, Oct. 16, 1945, —— I. C. C. —— and Order herein by the District Court dated November 9, 1945.

makes no difference how the elements of value to which the Commission and the District Court looked in this determination may be shifted from one form to another, for in each successive form they remain the property of those who receive the new securities under the Plan. Thus, if cash is invested in improvements to the property, as is in fact done continually, it could not be said that anything has happened to upset the Plan. Nor yet if cash is used, as it often is, for the purchase of Government bonds. There is no difference, we submit, where cash is used to reduce outstanding claims in such manner that the new company is relieved from a current burden and provided with an additional asset (here the increased equity in the equipment and the full ownership of the Junction Company). The holders of new securities under the Plan are entitled to the cash. They are entitled, indeed, to receive all of it as a distribution of interest and dividends on the new securities. Their rights can surely be no less because of a choice by the operating management to apply the cash for the benefit of the road, whether in property improvements or in reductions of debt."

Consummation of the Plan in such circumstances will give the benefit of this value, in whatever form at the moment represented, to those entitled under the Commission's Plan, and in the same proportions. The Circuit Court shifts those proportions, by increasing the share of a junior interest, because of the mere chance of the particular use, among many conceivable uses, to which cash on hand after the stated effective date is put. Such slavery to form was rejected in the Southern District of Illinois in the important Rock Island reorganization upon paying off the large debt to RFC involved in that case:

> "Clearly the payment of a claim or the purchase of securities would not afford a basis for a redistribution of securities allotted under the plan. It would amount merely to appropriating surplus earned since the effec-

tive date of the plan to one of the several uses to which it could be applied. All those who have interests, as stockholders of the reorganized company in the earned surplus would benefit from such a use of the money consistently with the plan, just as they would if the money were spent for additions and betterments or used after the consummation of the plan to purchase securities. If there were a redistribution of the securities that would not be true." (*In re Chicago, Rock Island and Pacific R.*, —— F. S. —— (N. D. Ill. 1945), C. C. H. Bankr. L. S., ¶55,369)

The Circuit Court, therefore, had no justification for overriding the Commission's determinations of public interest and private right. On both grounds its order should be reversed so that, in this respect also, the orders establishing the Plan may be affirmed.

IV
UTAH FUEL STOCK

(a) Introduction

This is a harrower issue. It is whether a system bondholder (of the Western Consolidated Bonds) who has also a first lien on property (namely stock in Utah Fuel Company) owned by others than the Debtor may receive new securities in respect of his total claim and thereafter proceed against the collateral for any deficiency (as the Plan permits[25]), or whether he must first reduce his claim by some amount for the collateral and then receive new securities only for the balance (as the Circuit Court requires).

[25] R. 20-21, 136, 167. Clearly, however, the Plan does not mean that they may receive, in the aggregate, more than the amount of their claim.

(b) THE FACTS.

Utah Fuel Company is a New Jersey corporation with a capitalization of 100,000 shares of stock (R. 1114, Ex. 253). It was organized in 1900 and acquired various coal properties in Utah in territory served by the Rio Grande (*id.*). Production was originally at a substantial figure, but declined from an average of nearly 2,000,000 tons a year in 1913-21 to less than half that figure in the 'thirties (*id.*, p. 23), reflecting a sharp increase in competition (*id.*, p. 25)[26]. During the eight-year period 1922-1929, earnings, though fluctuating sharply, averaged $317,000 a year after depreciation (*id.*, p. 95). During the seven-year period 1930-36, average earnings were a deficit of $10,000 a year (*id.*, p. 97).[26] A total going concern value at the 1936 year-end of $4,650,000 was estimated (*id.*, p. 33). There is no testimony supporting a higher value, and there is no testimony at all that any such price could be realized in the market. No dividends have been paid since the 1924 reorganization of the Debtor except $250,000 paid in 1934, which was paid, despite a failure to earn any net income for six years, out of depletion cash, at a time when the Debtor was struggling to avoid bankruptcy; one-third of that amount was, in the opinion of the Debtor's witness, adequate recognition of annual earning power:[27]

> "In determining a proper allowance to make the RGW Consol's for this stock, neither the earnings of the company in the past, nor the book value of its property at the moment, furnish a suitable base." (R. 1102)

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[26] In the extraordinary conditions of war time, earnings have been much higher: $415,000 for 1942 and $536,000 for the first seven months of 1943 (R. 1052).

[27] R. 1102, 713.

The Western Consolidated Mortgage is an indenture executed by The Rio Grande Western Railway Company under date of April 1, 1899, to secure an issue of its First Consolidated Bonds (R. 1079, Ex. 34, D. Ct. Pro. 806). Utah Fuel Company was not in existence at that time. The mortgage, however, provided that among the additional bonds that might be issued thereunder were bonds in an amount not exceeding 10 million dollars which might be issued from time to time "to pay for acquisitions lawfully made with a view of increasing its traffic or earnings" (R. 1079-80).

By an agreement of May 23, 1901 (R. 1080, Ex. 34j), between Spencer Trask & Company, the Rio Grande Western and the Indenture Trustee, the first of these parties, reciting that it then owned all the Utah Fuel stock, pledged it with the Indenture Trustee "in all respects subject to the terms and conditions of said mortgage" (but with a right of redemption upon depositing with the Indenture Trustee 6 millions in cash or in Western Consols) and assigned the equity of redemption to the Rio Grande Western. Against this pledge 6 million dollars principal amount of Western Consols were issued,[28] for the evident purpose of providing payment for the stock.

In 1908 the Rio Grande Western was consolidated with The Denver and Rio Grande Railroad Company (1886) to form a new corporation under the latter name. Upon default of certain Western Pacific bonds guaranteed by the 1886 company, a deficiency judgment for an amount ultimately exceeding 40 million dollars was obtained against the consolidated company.[29] Its properties were sold in execution

[28] *Denver and Rio Grande Railroad Company*, 26 Val. Rep. 733, 888 (1929).

[29] See *Equitable Trust Company* v. *Western Pacific Ry.*, 244 F. 485 (S.D.N.Y. 1917) and *Equitable Trust Company* v. *Denver and Rio Grande R.*, 250 F. 327 (C.C.A. 2, 1918).

of that judgment on November 20, 1920.[30] The purchasers conveyed the railroad properties to the Debtor,[31] and all its stock was issued to The Western Pacific Railroad Corporation. The Utah Fuel stock, however, was transferred by the purchasers, subject to the lien of the Western Consolidated mortgage, to The Western Pacific Railroad Corporation (R. 1082, Ex. 35). The Debtor never acquired title.

The Debtor could not sustain the burden of the debt left on it in that reorganization. Receivers were appointed in 1922 and a further reorganization (R. 1083) was consummated in 1924.[32] As a part of that plan the Missouri Pacific acquired half of the Western Pacific holdings, not only in stock of the Debtor but also in the Utah Fuel stock. As an inducement to bondholders not to disturb the old stock of the Debtor, they put up their interest in the Utah Fuel stock as additional security under the two new mortgages created in that reorganization. This was done by an agreement of December 20, 1924 (R. 1081, Ex. 35). The two new mortgages were the R&I Mortgage, to provide for new financing, and the General Mortgage, to provide for some of the old debt. The words were that the Missouri Pacific and the Western Pacific, while reserving to themselves "the ultimate beneficial interest in said 100,000 shares of the capital stock of Utah Fuel Company" (*id.*, R. 1084), assigned their interest to a trustee so that dividends on it should be paid to the Debtor so long as any bonds issued under the new mortgages (or any other bonds issued to refund them)

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[30] See *Equitable Trust Co.* v. *Denver and Rio Grande R.*, 269 F. 987 (D. Col. 1920); *Levy* v. *Equitable Trust Co.*, 271 F. 49 (C.C.A. 8, 1921); *Beer's* v. *Equitable Trust Co.*, 286 F. 878 (C.C.A. 8, 1923) and *Beers* v. *Denver and Rio Grande R.*, 286 F. 886 (C.C.A. 8, 1923).

[31] See *Stock of Denver and Rio Grande Western Railroad*, 70 I.C.C. 102 (1921).

[32] See *Denver and Rio Grande Western Reorganization*, 82 I.C.C. 745 (1923) and 90 I.C.C. 141 (1924) and *Denver and Rio Grande Investigation*, 113 I.C.C. 75 (1926).

should be outstanding, unless the Debtor's net income should exceed stated limits (*id.*, R. 1084-85). It was further provided that upon foreclosure of the mortgage securing any such bonds, the assignors' interest in the Utah Fuel stock should, subject to the lien of the Western Consolidated Bonds, be sold, and the proceeds be applied to the payment of such bonds, any surplus to be divided equally between the Missouri Pacific and the Western Pacific (*id.*, R. 1089-90).

While the Debtor joined in this agreement as a formal transferor in order to avoid any question of title arising from the reorganization, it is perfectly clear that the Debtor did not then have, and did not thereby acquire, any interest in the Utah Fuel stock. As the Commission, in authorizing the consummation of the Plan, declared:

> "... the applicant [the Debtor] neither owns, nor under the plan of reorganization is to acquire ownership of, the stock of the Utah Fuel Company ..." (*Denver and Rio Grande Western Reorganization*, 90 J. C. C. 141, 148 (1924))

The transaction was only that the equity of redemption in the Utah Fuel stock was put up by its owners as additional security for the new bonds created in reorganization, as part of the consideration to creditors for not disturbing the equity. This subjection of the stock by its pledgors to the liens of additional mortgages of the Debtor was not intended to transfer the equity of redemption from the pledgors to the Debtor.* On the contrary, in the operative words of the parties themselves, "the ultimate beneficial interest" remained with the Western Pacific and the Missouri Pacific.

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* The Debtor has never recorded the Utah Fuel stock on its books but has uniformly recorded the 1924 contract at $1 (Ex. 25-B (I Tr. 2839) and I.C.C. Tr. 137-8 (I Tr. 2064-65); "Income Account and Financial Exhibit" for December 31, 1944, p. 7.)

(c) The Law

Since the Utah Fuel stock is not property of the Debtor, it is not subject to disposition under Section 77, for that deals only with the "debtor and *its* property".[34] The Commission therefore properly left the Utah Fuel stock subject to pledge under the Western Consolidated Mortgage.

In doing so, the Commission followed the controlling precedent of this Court's decision in the *Western Pacific Case*. There the Commission held that the plan should be framed as

> "in no wise disturbs or alters the rights of the Reconstruction Finance Corporation and the Railroad Credit Corporation in collateral pledged with them by parties other than the debtor." (*Western Pacific Railroad Company Reorganization*, 230 I. C. C. 61, 102 (1938), and to the same effect at 233 I. C. C. 409, 432 (1939)).

Accordingly its plan (233 I. C. C. at 453) left the collateral undisturbed. As this Court said:

> "This collateral . . . was therefore left with the pledgees with its position unaffected by any direct action of the Commission." (*Western Pacific Case*, 318 U. S. at 506 (1943))

Under the decision The Railroad Credit Corporation received new securities in respect of the full amount of Western Pacific bonds pledged with it, without any reduction because of estimated realization from the collateral pledged with it by others, and retained its full rights in such other collateral. Later the District Court in charge of the properties permitted The Railroad Credit Corporation to receive the payments made to it on such other collateral, over the objection of the Debtor that the award of new securities to it in the plan had made it whole, because:

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[34] Section 77(a), italics added.

". . . the market value of the [new] securities is much less than their face value . . . and it will not be able to realize thereon enough to satisfy its claim. . . ."

In the case at bar the Commission scrupulously followed the Western Pacific precedent, for extra caution spelling out the powers of the pledgee rather than merely leaving them implicit as in the *Western Pacific Case*. In result, the Western Consolidated bondholders remained free to realize on the Utah Fuel stock by future proceedings. But of course the Western Consolidated bondholders may not obtain a total realization, measured by actual value, that exceeds the amount of their claim.[36] So when enforcement of the pledge by distribution or sale is sought, and the Western ConsolidatedTrustee acknowledges that it can be sought only through judicial proceedings, it will be appropriate in those proceedings to inquire whether such action will result in any excess realization. Full protection can then be given to all those who have any junior interest in the stock. Though it may be thought obvious that no such overpayment could in fact result,[37] that question has not arisen, for the Indenture Trustee has not yet taken any move to accomplish the distribution or sale of the stock. Until then, there is no question to consider.

But the fact that future realization on the collateral of others will be limited by the actual value received from the

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[35] *In the Matter of The Western Pacific Railroad Company*, N. D. Cal. S. D., No. 26,591-5, June 21, 1944 (unreported), *aff. sub nom The Railroad Credit Corporation* v. *Ecker*, —— F. 2d —— (Dec. 7, 1945, C.C.A. 9). That is the case here, for, as shown in Appendix G, the Western Consolidated bondholders receive, on the basis of when issued quotations, only about two-thirds of their total claim.

[36] *Merrill* v. *National Bank of Jacksonville*, 173 U. S. 131 (1899).

[37] The Plan takes from the Western Consols the high leverage of their position on the western half of the system, junior only to the First Trust 4's (as a result of which the earnings applicable to them per bond increase sharply once the Trust's are covered) and gives them in return only 20% in Income Bonds, 73% in Preferred Stock and 7% in Common (R. 182).

estate does not mean that the realization from the estate is to be limited by what may later be received on such collateral. Just the contrary was held in the *Western Pacific Case*. The decision in that respect applied the unbroken rule that in such cases the collateral creditor need not deduct the value of his collateral in distributions from the estate (which allocations of new securities are) but may receive recognition out of the estate on the basis of the total amount of his claim and thereafter realize upon his collateral up to an aggregate actual value equalling the amount of his claim.

This was the settled rule in equity reorganizations (*Merrill* v. *National Bank of Jacksonville*, 173 U. S. 131 (1899)), the basic principle being that

> ". . . no part of his security can be taken from a secured creditor until he is completely satisfied." (138)

In bankruptcy proceedings a different rule was laid down with respect to collateral owned by the bankrupt, but only for property so owned. Thus Section 1(28), 11 U. S. C. Sec. 1(28), defines "secured creditor" as including

> ". . . a creditor who has security for his debt *upon the property of the bankrupt* . . . or who owns such a debt for which some endorser, surety, or other person secondarily liable for the bankrupt has such security upon the bankrupt's assets;" [italics added.]

Dealing with this defined term, Section 57(h), 11 U. S. C. Sec. 93(h), provides:

> "The value of securities held by secured creditors shall be determined by converting the same into money according to the terms of the agreement pursuant to which such securities were delivered to such creditors, or by such creditors and the trustee by agreement, arbitration, compromise or litigation, as the court may direct, and the amount of such value shall be credited

upon such claims, and a dividend shall be paid only on the unpaid balance. Such determination shall be under the supervision and control of the court."

Though the procedure specified in this Section for a determination of value is clearly inapplicable in railroad reorganizations, the Commission being designated for that purpose,[36] it has been held that the remainder of this Section, that is, the requirement that the value of the collateral shall be credited upon the claim before determining distributions from the estate, applies under Sec. 77 (*New York Trust Co.* v. *Palmer*, 101 F. 2d 1, 3 (C.C.A. 2, 1939)).

But it is clear, by the very words of the Act, that this requirement applies only to "security . . . upon the property of the bankrupt." It is always recognized that no deduction is required for the value of collateral which is not "the property of the bankrupt," but is the property of some one else, for in that situation the rule in equity proceedings, being unchanged by the statute, prevails in full force.[37] The rule is well shown by the following quotation:

"Unless the petitioner was a secured creditor as defined by §1 (23) [presently §1 (28)] it was not bound

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[36] The last paragraph of Sec. 77(e) provides that:

"If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan."

[37] Illustrative citations are:

Ivanhoe Building & Loan Association v. *Orr*, 295 U. S. 243, 245 (1935);

Swarts v. *Fourth National Bank*, 117 F. 1, 12 (C.C.A. 8, 1902);

Gorman v. *Wright*, 136 F. 164, 165 (C.C.A. 4, 1905);

Board of County Comr's. v. *Hurley*, 169 F. 92, 95, 97 (C.C.A. 8, 1909);

In Re New York Commercial Co., 233 F. 906, 909 (C.C.A. 2, 1916);

In Re United Cigar Stores Co., 73 F. 2d 296, 298 (C.C.A. 2, 1934), *cert. den.* 294 U. S. 708 (1935);

(*continued on next page*)

to have its security or the avails thereof valued and to prove only for the difference between that value and the face amount of the debt. Petitioner does not come within the definition, for at the date of bankruptcy it held no security against the bankrupt company's property, nor security given by any other person who in turn was secured by the bankrupt's assets. Sections 1(23) and 57(e) [11 U. S. C. §93 (h)] do not, therefore, forbid the proof of a claim for the principal of the bond with interest, though the petitioner may not collect and retain dividends which with the sum realized from the foreclosure will more than make up that amount." *(Ivanhoe Building & Loan Association* v. *Orr*, 295 U. S. 243, 245-6 (1935)).

As collateral in which the equity of redemption belongs to others does not become "property of the bankrupt" because pledged for one obligation of the bankrupt, so it does not when pledged for two or more obligations of the bankrupt. As this is true in the former case without regard to relative values, so it is also in the latter case. None of these factors has any relation to the policies of the rule. A policy of the rule is that creditors of the bankrupt who have a lien on property of others shall be entitled to full recovery on their total claim against the bankrupt without being forced to give other creditors a virtual participation in their security. The Western Consolidated bondholders are entitled to assert that statutory right whether they have the only lien, or whether junior lienors exist, and whether they will, upon foreclosure, be entitled to the whole of such collateral or will leave behind some surplus to be divided among junior claimants according to the same rules and subject to the same limitations. Those questions pertain only to the

In Re Fay Stocking Co., 95 F. 2d 961, 962 (C.C.A. 6, 1938);
In Re Headley, 97 F. 765, 771 (W.D. Mo. 1899);
In Re Blizard, 20 F. S. 481, 482 (E. D. Penn. 1937);
In Re Guilliot, 37 F. S. 929, 931 (W. D. La. 1942).

methods to be followed when foreclosure upon the outside collateral shall hereafter be attempted, and do not, as the General Mortgage Trustee erroneously argues,[40] have any bearing on the distribution to be made from the estate by allocations of new securities in the Plan. All those questions may be faced at the time of subsequent foreclosure upon the collateral in the judicial proceedings to be taken for that purpose.

Manifestly, therefore, it was proper, and indeed necessary, for the Commission to allot new securities to the Western Consolidated Bonds in respect of their total claim without any deduction because of the Utah Fuel stock while at the same time permitting later enforcement of all rights under the instruments of pledge.

Some suggestion is made here by the Debtor that the parties have agreed on the reverse of the above procedure.[41] But this suggestion is erroneous. The indenture supplemental to the Western Consolidated Mortgage, executed at the time of the pledge in 1901 (R. 1080), contains no provision remotely relating to this subject, nor does any other supplemental indenture to that mortgage. The agreement cited by the Debtor is the agreement of 1924 by which the Western Pacific and the Missouri Pacific subjected their equity of redemption in the Utah Fuel stock to certain terms of the R&I and the General Mortgage that were being concurrently executed. As shown above (p. 93), those rights included the privilege on the part of the indenture trustee under each of those two mortgages, in that order of priority, or under any mortgage executed to secure bonds for the purpose of refunding the bonds secured by them, to realize on the equity of redemption in the Utah Fuel stock, subject to its prior pledge under the Western Consolidated Mort-

[40] Brief in opposition to certiorari, pp. 17-18.

[41] Debtor's brief in opposition to certiorari, p. 7.

gage. In that connection the 1924 agreement (R. 1090) empowered such indenture trustees, or a preferred stockholders' committee therein named, to require realization under such mortgages upon the equity of redemption in the Utah Fuel stock before foreclosure sale of the railroad. But this has nothing whatever to do, and could not possibly have, with the vested rights of the Western Consolidated bondholders for the enforcement of their mortgage.

There is, accordingly, no contractual reversal of the ordinary rule, the cited provision of the Plan is proper and the action of the Circuit Court should in this respect also be reversed so that the orders establishing the Plan may be affirmed.

V

THE POWER TO CONFIRM OVER A DISSENT

(a) The Question

As a result of the 1935 amendment, Section 77(e) provides that upon approval of a plan by the District Court, it shall be submitted to all affected classes of security holders, except those whose interests are not of value, for their acceptance or rejection. If more than two-thirds in amount of those voting in each such class accept the plan, the judge shall confirm it if satisfied as to the legality of the voting, without re-examination of the merits of the plan.[42] The Act then proceeds:

> ". . . if the plan has not been so accepted . . . the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing [*i*] that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; [*ii*] that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and

[42] Next to last paragraph of Section 77(e).

all the relevant facts; and [*iii*] that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e):"[a]

Upon submission of the Plan in this case, it was accepted by the statutory percentages of all such classes except the General Mortgage Bonds. They rejected the Plan. This dissent represented 4.1% of all affected secured indebtedness, or 8.3% of all claims actually voted (R. 267). It represented 17.1% of the outstanding General Mortgage bonds, though, since only 21.5% of them were voted, it was 79.3% of those voted.

After the hearing, the District Court made the statutory findings and confirmed the Plan over this dissent (R. 224).

On appeal to the Circuit Court, the General Mortgage Trustee urged that (*a*) the Act, properly interpreted, does not purport to authorize confirmation over such a dissent (particularly a dissent by a majority of those voting) and (*b*) if so interpreted, the Act is unconstitutional.

The Circuit Court, at the conclusion of its opinion, held:

> "It follows from what has been said that the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, and that the District Court was without authority to confirm the plan in the face of their adverse vote." (R. 253)

This is the first holding that a dissenting class has a right of veto. The holding is obscure, for its grounds, and the resulting limits of its applicability, are not stated.

If it were true, which we submit it is not, that the Plan fails to satisfy the fair and equitable requirements of the Act, then, on that ground, it would follow that the District

[a] Next to the last paragraph of Section 77(e). Roman numbering interpolated.

Court, being obliged, in the event of a dissent, to find again that those requirements of the Act have been satisfied, may not confirm the Plan. But it is important, we believe, that this be established as the only test. If the Plan is fair and equitable (as the preceding discussion submits and as for present purposes we take it to be), no one can have a right of veto as a means of bargaining for preferential treatment. That is true, we submit, as a matter both of statutory construction and of constitutionality.

(b) Statutory Construction

The main purpose of the 1935 amendment, as we pointed out at page 37 above, was to eliminate the practical right of veto that was considered to vest in security holders under the original Act. Of the two means chosen for this purpose, the simplified test of value for reorganization purposes and the power to confirm over a dissent, the former was discussed there. The latter is decisive here. Of the two, the power to confirm over a dissent is the more critical, for it is the key to the whole Congressional plan for workable legislation. Thus the proposal was recommended to the House Judiciary Committee by Joseph B. Eastman, then Federal Coordinator of Transportation and proponent of the amendments, with this explanation:

> "Perhaps the most serious defect is that it was not realized when the act was passed to what extent it put it in the power of nonassenting classes of security holders to prevent a reorganization."[44]

It was just for the purpose of eliminating that veto power that the quoted provision was proposed and enacted. As Leslie Craven, counsel for Mr. Eastman and draftsman of the bill, explained to the House Committee:

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[44]Hearings before the Committee on the Judiciary on H. R. 6249, 74 Cong., 1st Sess. (1935) p. 15.

". . . the effect of those provisions is this, that if a plan is not approved by the requisite two-thirds of a class, the judge may nevertheless confirm the plan if he finds, after hearing, that it conforms to those requirements . . .

"In other words, in those cases where it is not possible to get the necessary percentage of assents, the court under these defined conditions can require that they take such provision as the plan provides for them . . ."[45]

The substantive principles incorporated in the Act are the numbered clauses in the quotation on pp. 100-1 above. Clause [*i*] requires only that the plan make "fair and equitable" provision for dissenters. Its obvious purpose was to outlaw the old equity practice of providing less for dissenters than for assentors. No question arises under it here. Clause [*iii*] lays down the basic requirement that the plan itself be "fair and equitable." For the purposes of the present question we assume this to be satisfied, as we have submitted above that it in fact is, and no question under it is pertinent here. Clause [*ii*] requires that the dissent be "not reasonably justified." The meaning of that language is the only question presented here.

Of course one should read "text in the light of context".[46] These words are colored by their setting in the Act, and alike by its policies. They preclude any interpretation that would revive the old veto power which it was a leading purpose of the Congress to extirpate. But it would be effectively revived by any interpretation that would permit a class of security holders to reject, and thus block, a plan unless they received something more than "fair and equitable" treatment, whether the improved treatment is characterized as superior to the "fair and equitable" provision or merely as lying at so high a level within the permissible area of Commission

[45] *Id.*, p. 339.

[46] *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 351 (1943).

judgment of what constitutes "fair and equitable" provision that no reasonable person could reject it. In the first alternative, all action is paralyzed, for no plan could lawfully award any class more than what is "fair and equitable", yet each class could veto it unless it did. In the second alternative, which seems to be the contention of the General Mortgage Trustee, the court would have to accord to the judgment of security holders as expressed in their vote somewhat the same effect as to the findings of an administrative agency, and thus be compelled, by equal and opposite forces, to reject the plan and to confirm it. Either interpretation nullifies the Act. Under either one, each class would be entitled to jockey with the Commission for a better track and the administrative findings to which the Congress looked in such large measure for the settlement of reorganization problems would merely signal to the post for that unseemly spectacle. It is contrary to the policies of the Act to encourage dissents by the stimulating expectation that a dissent will procure anything better than "fair and equitable" treatment.[47]

So clause [*ii*] can not, consistently with the policies of the Act, contemplate any standard other than that of a fair and equitable plan. Its effect is that the District Court, when required by a dissent to reconsider the merits of a plan, shall do so "in the light of the respective rights and interests of those rejecting it and all the relevant facts." For one thing this means that the District Court, while still judging the plan as of the "time of the finding" by the Commission, shall do so in the light of later events to the time of confirmation.[48] For the rest, it is surely relevant to observe that the General Mortgage Bondholders are the most junior lien and get everything left after giving the Senior Claims only an equal

[47]Thus see *Mason* v. *Paradise Irrigation District*, —— U. S. —— (1946).

[48]See also the discussion of this point beginning at p. 37 above.

face amount of new securities, though it has not been found and can not be assured, that such treatment will approximate payment of all the Senior Claims.

Respondents are misled by the mere mechanics of the voting into rigid concepts that defeat the Congressional purpose. The voting is not, as they urge, a useless gesture unless it operates to give some power to veto. On the contrary, it requires a reexamination of the merits of the plan by the court and throws a spotlight on the situation of any particular class that may dissent, thus aiding the court to focus on the pertinent questions. This was clearly put to the Judiciary Committee by Mr. Eastman himself, in words we think decisive here, not only as an episode of legislative history, but also as a formulation of the applicable policies:

> "Nothing can be forced upon them without an adjudication of their rights in accordance with sound principles which are definitely stated in the bill, and by two tribunals, the Commission and the court; and before any such adjudication is made, they are given opportunity not only to argue their rights and to submit what evidence they may desire to submit at public hearings, but to vote upon any plan before it is made effective, in order that the court may be fully informed in regard to the position of each and every class of security holders, whether they be debtors or creditors."[49]

Of course the Act draws no distinction, in this power to confirm over a dissent, according to the percentages of the vote, whether the dissent is a minority of the vote, or a majority of the vote or the whole of the vote, but confers the power equally in all situations of the vote. Nor can the fair and equitable standard of the Act be varied by the fact, much urged below by the General Mortgage Trustee, that there has been pending for some time before the Congress a pro-

[49] Hearings before Committee on the Judiciary on H. R. 6249, 74th Cong., 1st Sess. (1935) 282.

posal, known as the Hobbs Bill, to change the Act, for that proposal has not been adopted.[50]

(c) Constitutionality

The argument of the General Mortgage Trustee on the constitutional point is that, upon a dissent by a majority of the voted General Mortgage bonds, those bondholders are constitutionally entitled to obstruct the will of the Congress and the concurring judgment of the Commission and the District Court that the plan is fair and equitable, in order, so it would seem, that the General Mortgage bondholders may suffer the fate plainly awaiting them in equity practice of being sold out in foreclosure of senior liens.

In properties of this size a foreclosure sale has uniformly been recognized as a mere device to accomplish predetermined reorganization aims.[51] It is not realistic to suppose that the most junior lienor can derive any substantive advantage from that technique. Nor is there now any arguable constitutional question about the power of the Congress to substitute improved remedial methods.

This question was presented to this Court on application for certiorari to the Seventh Circuit to review the affirmance of a decree confirming a plan over the dissent of 49.63% of those voting in one class[52] and certiorari was denied. Clearly the Court did not consider that any substantial constitutional question was presented and its action is generally

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[50] Adopted by the House on a favorable report from the Committee on the Judiciary (H. R. Rep. No. 1615, 78th Cong., 2d Sess. (1944)), but still pending in Committee in the Senate.

[51] *Canada Southern R.* v. *Gebhard*, 109 U. S. 527, 539 (1883); Paul D. Cravath, "The Reorganization of Corporations", "Some Legal Phases of Corporate Financing, Reorganization and Regulation", p. 153 at 204-5 (1916).

[52] *In re Chicago and North Western R.*, 126 F. 2d 351 (C.C.A. 7, 1942), *cert. den.* 318 U. S. 793 (1943).

thought of as ending all constitutional doubt.[53] The Circuit Court of Appeals had quoted with approval the following statement of the District Court:

> ". . . the power to confirm a composition over the objection of 33 1/3% of the creditors is exactly the same kind of a power as the power to confirm a composition over the objection of 49.63%, or for that matter over the objection of 100% of them. It is a bankruptcy power."[54]

Since then the District Court for the Eastern District of Missouri has ruled similarly, in a case where the plan was rejected by a majority of the voted claims in six classes:

> "We can conceive of a situation where one or more classes of creditors would vote against a plan even though it had met all legal requirements including those of fairness and equity. According to the contention here made, the Court cannot override the creditors veto and the reorganization process might be continued indefinitely and perhaps forever. This is not to be countenanced. Against the public interest, even a large group of creditors may be considered to be but a dissident and obstructive minority." (*In re Missouri Pacific R.*, 50 F. S. 936, 943 (E. D. Mo. 1943)).[55]

This is in accord with sound principle. A mortgagee is constitutionally entitled to some substantial access to the benefit of his security,[56] but not by any particular procedural methods, for they may be revised as the Congress

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[53] *E.g.*, Robert T. Swaine, *A Decade of Railroad Reorganizations under Section 77 of the Bankruptcy Act* (1943) 56 Harv. L. Rev. 1037, 1053.

[54] *Id.*, at 126 F. 2d 365, n. 9.

[55] Similar views had been declared also in *In re New York, New Haven & Hartford R.*, 16 F. S. 504, 509-12 (D. Conn. 1936).

[56] *Louisville Joint Stock Land Bank v. Radford*, 295 U. S. 555 (1935).

thinks appropriate in the public interest.[57] Thus the Congress may abolish the right of foreclosure where the mortgagee is paid the value of the property as found by the court:

> "Safeguards were provided to protect the rights of secured creditors, throughout the proceedings to the extent of the value of the property . . . There is no constitutional claim of the creditor to more than that." (*Wright* v. *Union Central Life Insurance Co.*, 311 U. S. 273, 278 (1940); *rehearing den.*, 312 U. S. 711 (1941)).

If an award of cash found to be the value of the lien position satisfies all constitutional rights in the case of an average-sized loan to an individual, an award of new securities found to be the equitable equivalent of the existing position must do so in the case of a large interstate railroad, where outside purchasers are unobtainable and new securities are the customary medium of satisfaction.[58] Opposition by all members of the affected class must, therefore, be as constitutionally meaningless in the latter case as in the former. No other conclusion would accord with the public interest in railroad reorganizations[59] or with the "radically progressive nature" of the bankruptcy power.[60] Nor would any

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[57] *Wright* v. *Vinton Branch*, 300 U. S. 440 (1937), limiting the case cited in the next preceding footnote.

[58] So held even in the absence of enabling legislation in *Phipps* v. *Chicago, Rock Island & Pacific R.*, 284 F. 945 (C.C.A. 8, 1922).

[59] Craven and Fuller, *The 1935 Amendment of the Railroad Bankruptcy Law* (1936) 49 Harv. L. Rev. 1254, 1279-81.

[60] *Continental Illinois National Bank* v. *Chicago, Rock Island & Pacific R.*, 294 U. S. 648, 671 (1935). And see *Gilfillan* v. *Union Canal Co.*, 109 U. S. 401, 404 (1883), holding that a statute may constitutionally presume the assent of security holders who do not vote; under such a presumption, a majority of the General Mortgage bondholders have accepted the Plan. Due process "demands only that the law shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be attained." (*Nebbia* v. *New York*, 291 U. S. 502, 525 (1934).

other conclusion accord with the settled rule that by such proceedings a creditor may be denied all recognition (*Western Pacific Case*, 318 U. S. at 476), for the power to deny includes the power to limit.

We submit, therefore, that there is no constitutional obstacle to full effectuation of the Congressional will that a court, reconsidering a plan in the light of a dissent and again finding it fair and equitable, may confirm the plan and the dissenters have no right of veto.

CONCLUSION

The Circuit Court, we submit, errs in each of the particulars in which it requires a change in the Commission's Plan. Its order, therefore, should be reversed in its entirety, with instructions to affirm the orders of the District Court approving and confirming the Plan, so that this reorganization, already so long considered by the Commission and the courts, may move forward to its completion in accordance

with the Congressional policy of prompt action in these matters colored by the public interest.

Dated February 2, 1946.

Respectfully submitted,

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DENVER & RIO GRANDE WESTERN
RAILROAD
Rio Grande

APPENDIX B

Excerpts from Section 77 of the Bankruptcy Act As Amended.

(a) . . . If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose . . .

. . . . . .

(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requfrements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the

approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) hereof. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) hereof, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or re-

ports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: *Provided*, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further*, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency

or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Commission shall certify to the judge the results of such submission.

Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided*, That if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e): *Provided further*, That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of

the preceding paragraph hereof: *Provided further*, That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the plan, he shall enter an order and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

APPENDIX C

CAPITALIZATION AS OF JANUARY 1, 1943

Title of Issue	Principal	Interest at Contract Rate to Jan. 1, 1943	Total Claim	
RIO GRANDE				
Equipment Obligations	$ 5,758,000		$ 5,758,000	1
Trusts (R. G. W. First Trust 4's)	15,190,000	$ 4,860,800	20,050,800	
Western Consols (R. G. W. Consols)	15,080,000	4,976,400	20,056,400	
Junctions (R. G. J. 5's)				2
Eastern Consols (D. & R. G. Consols)	40,507,000	14,043,615	54,550,615	3
R&I's (Refunding and Improvement)	14,000,000	5,940,000	19,940,000	4
Generals (General Mortgage)	29,808,000	13,740,155	43,548,155	
R. F. C. Notes	10,691,850	3,208,755	13,900,605	5
Chase Bank Note	1,500,000	658,458	2,158,458	6
R. C. C. Note				7
Total Secured Debt	$132,534,850	$ 47,428,183	$179,963,033	
Unsecured claims	440,000		440,000	8
Total Debt	$132,974,850	$ 47,428,183	$180,403,033	
Preferred Stock ($100 par)			16,433,200	9
Common Stock (no par)			62,457,540	10
Stock Liability for Conversion—Preferred			12,400	
Total Stock			78,903,140	
Grand Total			259,306,173	
SALT LAKE				
First Mortgage Bonds	1,500,000		1,500,000	11
Income Mortgage Bonds	11,000,000		11,000,000	12
Common Stock (no par)			5,317,104	13
Total			17,817,104	
SALT LAKE WESTERN				
R F C Note	3,110,850	1,179,977	4,290,827	14
Common Stock ($100 par)			3,631,000	15
Total			7,921,827	

[Notes to this table appear on the following page.]

NOTES TO APPENDIX C

(1) Subsequently reduced by paying principal maturities of $609,000 a year. Currently being increased by a new issue of $2,610,000.

(2) $2,000,000 principal amount, with accumulated interest of $758,333, were outstanding at January 1, 1943, but were purchased by the Debtor Trustees pursuant to an Order of September 16, 1943 (R. 264), under which such bonds are held subject to further order of the District Court.

(3) In two series, 4% and 4½%; for details see Appendix D.

(4) In two series, 5% and 6%; for details see Appendix D.

(5) This claim is the total of three classes of notes:

(i) Five notes dated March 29, 1932—June 30, 1933 in the aggregate principal amount of $3,950,000 (bearing interest at 6%) to provide funds for interest, taxes, etc., secured by various system bonds and other collateral;

(ii) Various notes dated January 1933—August 1934 in the aggregate principal amount of $3,631,000 (bearing interest at 5%) to provide funds for construction of Dotsero Cut-Off, secured by all capital stock of the Salt Lake Western and by collateral under (*i*); and

(iii) One note dated December 19, 1934 for $3,110,850 (bearing interest at 5%) payable to bearer, issued to the Salt Lake Western to provide funds for purchase of Salt Lake stock and secured by all shares so purchased and by collateral under (*i*) and (*ii*); the funds were obtained by the Salt Lake Western from RFC against its own note of equal amount secured by said Rio Grande note and its collateral.

The collateral so held by RFC is:

ISSUE	PRINCIPAL AMOUNT
Trusts	$ 10,000
Western Consols	1,395,000
Eastern Consol 4's	783,000
R&I 5's	4,385,000
Salt Lake Incomes	1,266,000
Salt Lake Western stock	36,310 shs. (all of issued)
Salt Lake stock	45,889 shs. (91.8% of issued)

In addition RFC holds certain motorway stocks, Goshen Valley stock

and Rio Grande Southern R. bonds (taken up in plan at $250,000), a lien on the $662,000 of Eastern Consol 4's pledged under the R. C. C. Note and a second lien on the $6,096,000 of R&I 5's pledged under the Chase Bank Note, and certain contractual rights.

(6) Secured by $6,096,000 of R&I 5's. Interest computed at 6% after default (R. 141 and 21).

(7) Paid ($261,847.01 and interest) by Debtor Trustees on May 17, 1943, pursuant to an Order of April 15, 1943, under which such collateral was to be held so as to preserve without prejudice all rights of all security holders.

(8) Approximate; see R. 183.

(9) No dividends ever paid; 113½% accumulated dividends as of January 1, 1943.

(10) 300,000 shares of no par value, shown at amount stated on balance sheet. No dividends ever paid.

(11) Interest paid currently.

(12) Interest paid at less than stated rate, but no accumulations. $1,266,000 owned by Rio Grande and pledged with RFC (v. n. 5).

(13) 50,000 shares of no par value, shown at amount stated on balance sheet. No dividends ever paid.

(14) Held by RFC as shown in n. 5.

(15) Owned by Rio Grande and pledged with RFC as shown in n. 5. Properties operated under lease by Rio Grande, which receives all revenues from such operation.

APPENDIX D

RIO GRANDE BONDS

Total Claims as of January 1, 1943

	Principal	Unpaid Interest	Total Claim
OUTSTANDING			
G. W. Trust 4's	$ 15,190,000	$ 4,860,800	$ 20,050,800
G. W. Consol 4's	15,080,000	4,976,400	20,056,400
G. J. 5's	2,000,000	758,333	2,758,333*
& R. G. Consol 4's	34,125,000	11,602,500	45,727,500
& R. G. Consol 4½'s	6,382,000	2,441,115	8,823,115
& R. G. Consol 4's and 4½'s	$ 40,507,000	$ 14,043,615	$ 54,550,615
& R. G. W. R&I 5's	12,000,000	4,950,000	16,950,000
& R. G. W. R&I 6's	2,000,000	990,000	2,990,000
& R. G. W. R&I 5's and 6's	$ 14,000,000	$ 5,940,000	$ 19,940,000
& R. G. W. Gen 5's	29,808,000	13,740,155	43,548,155
PLEDGED			
RFC			
R. G. W. Trust 4's	10,000	3,200	13,200
R. G. W. Consol 4's	1,395,000	460,350	1,855,350
& R. G. Consol 4's	783,000	266,220	1,049,220
& R. G. W. R&I 5's	4,385,000	1,808,813	6,193,813
Total RFC	$ 6,573,000	$ 2,538,583	$ 9,111,583
R. C. C.			
& R. G. Consol 4's	662,000	225,080	887,080
Chase Bank			
& R. G. W. R&I 5's	6,096,000	2,514,600	8,610,600
OUTSTANDING AND PLEDGED			
R. G. W. Trust 4's	15,200,000	4,864,000	20,064,000
R. G. W. Consol 4's	16,475,000	5,436,750	21,911,750
R. G. J. 5's	2,000,000	758,333	2,758,333*
& R. G. Consol 4's	35,570,000	12,093,800	47,663,800
& R. G. Consol 4½'s	6,382,000	2,441,115	8,823,115
& R. G. Consol 4's and 4½'s	$ 41,952,000	$ 14,534,915	$ 56,486,915
& R. G. W. R&I 5's	22,481,000	9,273,413	31,754,413
& R. G. W. R&I 6's	2,000,000	990,000	2,990,000
& R. G. W. R&I 5's and 6's	$ 24,481,000	$ 10,263,413	$ 34,744,413
& R. G. W. Gen 5's	29,808,000	13,740,155	43,548,155
Total			$179,513,566

*Purchased later by Debtor Trustees.

App. E, F. 1

APPENDIX E

RIO GRANDE

NEW CAPITALIZATION UNDER PLAN (WITHOUT CONSOLIDATION)

Title of Issue	PRESENTLY TO BE ISSUED			To be Outstanding (1)	Annual Requirements
	To be Publicly Held	To be Pledged as Collateral	Total		
Equipment Trust Obligations	5,758,000		5,758,000(2)	5,758,000(2)	139,989 (2)
First Mortgage Bonds (3)	31,249,764	3,090,922(4)	34,340,686	32,816,610	1,030,220
Total Fixed Interest					1,170,209
Contingent interest on First Mortgage Bonds (5)					343,407
First Mortgage Sinking Fund					171,703
Total requirements before Second Mortgage Interest					1,685,319
Chase Bank Note				2,158,458	
Second Mortgage Bonds (6)	20,415,162	2,361,148(7)	22,776,310	21,803,312	1,024,934 (8)
Second Mortgage Sinking Fund					56,941
Total debt and requirements before Preferred Dividends				62,536,380	2,767,194
Preferred Stock (9)	32,120,120	5,076,089(10)	37,196,209	35,301,877	1,859,810(11)
Total requirements before Common Dividends					4,627,004
Common Stock (12)	35,167,585	8,081,104(13)	43,248,689	39,029,495	
Total Capitalization (excluding securities for Junction Bonds)	124,710,631	18,609,263	143,319,894	136,867,752	

NOTES TO APPENDIX E

(1) Includes RFC collateral, since the escrow agreement is not to be enforceable except through the collateral, but excludes Chase Bank collateral, since the note is to be enforceable as such.

(2) See n. 1 to Appendix C. Bear interest at 3¼%, 3% and 2%. Due serially 1946-1954.

(3) Bear fixed interest at 3% and prior contingent interest at 1%. Due 1993.

(4) $1,566,846 under escrow agreement with RFC and $1,524,076 under note to Chase Bank.

(5) No deduction is made for the Capital Fund since roadway depreciation under the accounting requirements effective from January 1, 1943, will apparently be charged in such amounts as to eliminate any obligation to the Capital Fund (see Rio Grande Annual Report 1943 p. 4).

(6) Bear contingent interest at 4½%. Due 2018.

(7) $1,388,150 under escrow agreement with RFC and $972,998 under note to Chase Bank.

(8) Of this amount $18,410 represents interest on Chase Bank collateral in excess of interest on the note and thus applicable under the Plan to the reduction of the principal of the note. Excluded from tax-deductions in Appendix F.

(9) 5% Preferred stock of the par value of $100 per share.

(10) $3,181,757 under escrow agreement with RFC and $1,894,332 under note to Chase Bank.

(11) All Preferred dividends on Chase Bank collateral ($94,717) are in excess of interest on the note and are thus applicable to reduction of its principal.

(12) Par value $100 per share.

(13) $3,861,910 under escrow agreement with RFC and $4,219,194 under note to Chase Bank.

NOTES TO APPENDIX F

As reported. The Salt Lake is omitted from this table; its inclusion would make no significant change in the results. The table includes the Junction Company and the Salt Lake Western, as well as all operations of the Rio Grande over the Salt Lake line pursuant to the Trackage Agreement.

The reported net available for interest on funded debt plus (*i*) reported Federal income tax accruals, (*ii*) reported interest on unfunded debt, and (*iii*) the increases to project the lower 1940 unit costs of operation back through the earlier years of the proceeding (see Ex. 262, R. 1133), eliminating inter-company items with the Junction Company and the Salt Lake Western, and including the accounting adjustments shown in Report of Bureau of Accounts. The increases per Ex. 262 are: 1936, $1,709,096; 1937, $3,625,147; 1938, $2,422,599; 1939, $1,131,428; total, $8,888,240. To include these increases, as the table does, increases the net earnings and thus favors the General Mortgage Trustee.

Federal income taxes are computed at 35% on the earnings shown in Column 2 after interest payable under the Plan, excluding all interest on equipment obligations.

The deductions are interest on the new bonds (excluding equipment obligations and securities for Junction Bonds), requirements for Capital Fund (before 1943 only) and Preferred Dividends at 5%. No deductions are made for sinking fund installments.

The only deduction made in this column is dividends at 6% on the new Common Stock.

This column adds back all the Federal income taxes deducted in Column 3 and thus shows what would be the result if there were no Federal income tax at all.

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APPENDIX F

RIO GRANDE EARNINGS APPLIED UNDER PLAN

	1	2	3	4	5	6
	Gross Revenues (1)	Earnings Available for Income Taxes and Return (2)	Net Earnings After Income Taxes @ 35% Available for Interest and Dividends Under Plan (3)	Balance After Preferred Dividends (4)	Balance After Common Dividends @ 6%	Col. 3 If There Were No Federal Income Tax
1921	32,621,419	3,753,175	3,272,617	d 1,735,754	d 4,330,676	d 3,850,11
1922	33,350,594	5,645,978	4,502,939	d 505,432	d 3,100,354	d 1,957,31
1923	34,587,497	3,317,573	2,989,476	d 2,018,895	d 4,613,817	d 4,285,72
1924	33,011,558	3,029,479	2,802,214	d 2,206,157	d 4,801,079	d 4,573,81
1925	33,629,463	7,229,249	5,532,065	523,694	d 2,071,228	d 374,04
1926	34,030,309	8,347,110	6,258,675	1,250,304	d 1,344,618	743,81
1927	33,121,169	6,995,895	5,380,385	372,014	d 2,222,908	d 607,39
1928	33,200,656	7,767,286	5,881,789	873,418	d 1,721,504	163,99
1929	34,828,669	9,309,932	6,884,509	1,876,138	d 718,784	1,706,63
1930	29,747,537	6,841,186	5,279,824	277,765	d 2,317,157	d 755,79
1931	23,484,818	5,312,095	4,285,915	d 559,576	d 3,154,498	d 2,128,31
1932	17,560,621	2,984,207	2,772,788	d 1,924,598	d 4,519,520	d 4,308,10
1933	17,112,794	3,456,210	3,079,590	d 1,696,601	d 4,201,523	d 3,824,90
1934	19,246,850	2,594,675	2,519,592	d 2,219,950	d 4,814,872	d 4,739,78
1935	20,944,230	2,559,571	2,496,774	d 2,285,087	d 4,880,009	d 4,817,21
1936	25,599,309	3,470,282	3,088,736	d 1,809,618	d 4,404,540	d 4,022,99
1937	26,781,992	3,538,826	3,133,290	d 1,794,631	d 4,389,553	d 3,984,01
1938	23,404,171	2,745,954	2,617,923	d 2,225,552	d 4,820,474	d 4,692,44
1939	25,073,039	3,137,948	2,872,719	d 2,012,478	d 4,607,400	d 4,342,17
1940	26,219,195	2,920,513	2,731,387	d 2,182,464	d 4,777,386	d 4,588,26
1941	31,572,624	4,655,209	3,858,939	d 1,149,432	d 3,744,354	d 2,948,08
1942	54,475,496	19,209,045	13,318,932	8,310,561	5,715,639	11,605,75
1943	70,194,002	18,699,441	12,987,690	8,729,319	6,134,397	11,846,14
1944	70,346,987	13,949,384	9,900,153	5,641,782	3,046,860	7,096,99
Total	784,144,999	151,470,223	118,448,921	1,618,770	d60,659,358	d27,638,05

d indicates red figure

APPENDIX G

When-Issued Prices Under the Plan

PRICES*

	1945	
	High	*Low*
First 3s-4s 1993	103½	90¼
Income 4½s 2018	79⅞	67¼
Preferred Stock	67⅝	53½
Common Stock	31½	23½

REALIZATION**

	% of total claim on basis of	
	High	*Low*
Western Trusts	97.2%	84.2%
Western Consols	67.5%	54.2%
Eastern Consols	65.1%	54.7%
R. & I.'s	57.7%	46.9%

*Monthly closing prices from Bank and Quotation Record, published by Commercial and Financial Chronicle.

**The new securities allotted in the Plan to each old bond are taken at the indicated prices and their total is then expressed as a percentage of principal and interest on that bond to the stated effective date of the Plan on January 1, 1943.

COPY

No.'s 278-282

JOINT REPLY BRIEF FOR PETITIONERS

MAR 4
CHARLES

IN THE

Supreme Court of the United States

October Term, 1945

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.,

Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

J. HOWARD McGRATH,
Solicitor General of the United States

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March 1, 1946.

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INTRODUCTION

The briefs for the Respondents merit no extended reply. Confining our attention to the essential issues, we leave unmentioned many auxiliary contentions, however unfounded, even the reiterated contention that prior compromise proposals of the parties themselves have the effect of admissions and that admissions establish a standard of reasonableness limiting administrative action. That contention sufficiently answers itself.

The essential issues are adequately put in our Opening Brief. We comment here only on certain points of fact that may be confused by statements in Respondents' briefs and on certain issues they seek to raise beyond those actually presented. These have to do with the state of the record (dealt with in 1 below), the history of earnings (dealt with in 2 below) and the Debtor's excursions into other fields (dealt with in 3 below).

1.
THE RECORD

The record was not closed in 1941, as the Debtor asserts (pp. 9 and 17). The last hearing before the Commission was at that time.* But while the case was under submission to the Commission, it received further evidence from the District Court taken at a hearing in October, 1942, dealing with the earnings, cash resources and cash requirements of the road (R. 981-1028). Both the Debtor and the General Mortgage Trustee were represented at this hearing (R. 981). In the course of it there were described the new sources of traffic developed in wartime and the revenue expected from them (R. 995-6 and 1016-17). It is significant that the Geneva steel plant was one of the principal new

*See our Opening Brief, p. 13.

installations described (R. 995), though said by the Debtor to have been "constructed after the formulation of the Plan" (Brief, pp. 25 and 38).

The current course of the affairs of the road was still later shown in evidence at a hearing before the District Court in April, 1943 (R. 1028-45). The Debtor and the General Mortgage Trustee were again represented. Among other matters, the evidence showed the earnings for the full year 1942 and the first three months of 1943, the current asset position and the trend of wages and taxes.

By direction of the District Court, the transcripts of both hearings were certified to the Commission. They were received by the Commission, considered by it in its "formulation of the Plan" and referred to in its report of June 14, 1943, approving the Plan (R. 142-3). In addition, by stipulation of all the parties, current financial statements and other material filed with the District Court were always before the Commission as a part of its record (R. 661, 789, 879).

Clearly, therefore, the Commission's record was a modern one and portrayed the current situation down to a date within sixty days of the time it approved the Plan.

The Debtor's objection against denial of its motion of May 1, 1943, for a rehearing before the Commission (Debtor's Brief, pp. 17-22) is not among the issues in the cases at bar, but is only among the potential issues under the Debtor's petition for certiorari, which has not been granted. Not only that, but, in the light of the above circumstances, it is plainly without substance. There was no reason for the Commission to have a further hearing, and its refusal to have one was a matter wholly within its unreviewable discretion (*I.C.C.* v. *Jersey City*, 322 U. S. 503 (1944)). In that case the Court so held in a rate case when public authorities asked a rehearing before the Commission, not merely for further argument (as the Debtor says, p. 21), but "'in

order that the said record be brought up to date' " so as to show the results of war-time earnings (322 U. S. at p. 509). In so holding the Court pointed out that *Atchison T. & S. F. R.* v. *U. S.*, 284 U. S. 248 (1932), relied on by two of the Respondents,* had been "promptly restricted . . . to its special facts" (322 U. S. at 515).

While on the subject of the record, we wish also to correct the statement of the Debtor (p. 26), made as one of fact, but actually a conclusion, and an erroneous one at that, with regard to the Utah Fuel stock. In our Opening Brief we pointed out that nothing in the agreement of 1924 (R. 1080) creating certain junior claims on the Utah Fuel stock for the benefit of the R&I Mortgage and the General Mortgage, in that order of priority, did, or could, in any way affect or vary the rights of the Western Consolidated Bonds through their first lien on that stock created many years before (Opening Brief, pp. 99-100). The privilege conferred by the 1924 agreement to proceed, upon foreclosure, against the Utah Fuel stock before proceeding against the fixed properties of the railroad was not, as the Debtor says (Brief p. 26), a requirement that such action "must" be taken, and had no relation whatever to the Western Consolidated Mortgage, whose rights are controlling upon review of the Plan. It is, therefore, irrelevant to the issue.

2.

EARNINGS

The Respondents emphasize the contention that the General Mortgage Bonds have, by impounding, a lien on earnings since the beginning of the trusteeship in an amount greater than their award of new Common Stock,** imply-

*Debtor's Brief, pp. 20-21 and MOP Brief, pp. 18-19.

**General Mortgage Trustee's Brief, pp. 16, 18, 44-45; Debtor's Brief, p. 22.

ing, perhaps, that the right to the income impounded thereby vested in favor of the holders of the General Mortgage Bonds. But all of the prior lien mortgage trustees, on behalf of senior lienholders, took substantially simultaneous steps to impound income with regard to each item of property on which the General Mortgage is a lien. Thus no income could be impounded for the benefit of the holders of the General Mortgage Bonds unless the Prior Lien debts were paid in full.

In fact, on the Respondents' own figures, there was a deficit after *interest alone* on senior bonds in every year of the trusteeship until the unprecedented war year of 1942, indeed a deficit that exceeded 16 million dollars. A unique combination of favorable circumstances in the next year (the extraordinary volume of traffic, the relatively lower level in the rising spiral of operating costs and the tax carry-over of earlier deficits) largely reduced this accumulated deficit by the end of 1942, though it still exceeded 3 million dollars. It is only if earnings after the effective date of the Plan on January 1, 1943, be taken into account that this deficit disappears. But that is precisely what the General Mortgage Trustee may not do. It is not entitled to special equitable recognition because of earnings after the stated effective date of the Plan, for if the Plan be otherwise within the powers of the Commission and the District Court, all these earnings equitably belong to the recipients of the new securities. In addition, of course, the Senior Claims have a first lien on those earnings not only for their accrued unpaid interest, but also for their matured principal, in an aggregate amount far exceeding the total earnings (our Opening Brief, pp. 66-67).

On the fundamental point of prospective earning capacity as illustrated by the record of operations in the past the General Mortgage Trustee presents a table of earnings that

is confusing (Brief p. 21). It is important that the defects in that table be recognized.

(*i*) The question under review is the validity of the Commission's action in limiting the total new securities to the amount provided for in the Plan. The relevance of past earnings, taken as one of the indications of earning capacity for the future, is the extent to which they are adequate, or inadequate, to provide a fair return on the new securities provided for in the Plan. That can be shown only by a comparison of those earnings with the amounts required for that purpose, as shown in Appendix F to our Opening Brief. It can not be shown by a comparison of past earnings with anything else, particularly with the amounts required for interest on the excessive debt capitalization of the past which the property has demonstrated its inability to support. Yet that is the only purpose of the General Mortgage Trustee's table and the only information that can be derived from it.

(*ii*) In order to reach a result favorable to its contentions, the General Mortgage Trustee extends the period of the study into the past beyond the termination of Federal control after World War I, though such prior years involved conditions so essentially different as to afford no guide to the expectable future. For one thing, the record shows that the Rio Grande was then predominantly an originating carrier, while now it is predominantly an overhead carrier (our Opening Brief, p. 5). It is well known that the rate structure in those days was entirely different from that of modern times, the competition of trucks, buses and private automobiles had not developed to modern proportions, passenger revenues were at levels never subsequently approached until the abnormal and non-recurring conditions of World War II, and operating expenses for maintenance during government operation were notoriously, though necessarily, inadequate. Over half the total earnings which

would appear from this table to have been available for interest on the General Mortgage Bonds in the past are derived from these years before 1921. The table is not informative until those years are excluded, as is done in Appendix F to our Opening Brief.

(*iii*) The General Mortgage Trustee's table wholly fails to make any provision for accrued unpaid interest on bonds admittedly senior to it in lien, but takes into account only the principal of those bonds. The amount of the unpaid interest on senior bonds at the stated effective date of the Plan on January 1, 1943 was 35 million dollars (Appendix D to our Opening Brief). This sum is so large that no table omitting it can be informative. Provision for this sum is made in the Plan and reflected in Appendix F to our Opening Brief.

(*iv*) The General Mortgage Trustee's table fails to make any significant provision for Federal income taxes, though earnings for the future will surely be subject to a heavy toll for that public purpose, not only because of the tax rates that will obtain but also because of the conversion, required by the public interest, of much of the old debt into stock.

With such infirmities, the General Mortgage Trustee's table is wholly uninformative.

None of these objections can be urged against our portrayal of the facts in Appendix F to our Opening Brief. Nor is it true, as the General Mortgage Trustee urges (p. 20), that our table depends on any hypothetical factors or assumptions. The only assumption it makes it that the Plan was in effect during the period under review, and that is a necessary assumption because the whole purpose of the table is to see to what extent the property could have supported the Plan in the past. Our assumption of a 35 per cent income tax

rate as illustrative of future possibilities is in no sense a condition to the validity of the table, for the table also shows that even without any Federal income taxes whatever, past earnings would not have been adequate to supply a fair return on the new securities already provided for in the Plan. The only significant adjustment we made in reported earnings was to increase them by about 9 million dollars in order to make up for what seemed a manifest understatement of earnings in 1936-39 due to the active prosecution of the improvement program in those years (Note 2 to Appendix F). But we made that adjustment only to show the case most favorably to the General Mortgage Trustee and willingly relinquish it, if desired, and thus increase the resulting deficit by the same figure of 9 million dollars.

Thus it is clear, we believe, that past earnings, under any realistic analysis, have been seriously inadequate to provide a fair return on the new securities already provided for in the Plan, and on that ground alone we submit there necessarily was evidence to support the Commission's determination of permissible new capitalization.

The menace of rising costs of operation for the future, a rise that seemed to us, on the record of many years, inexorable, is muffled by the General Mortgage Trustee under general reference to operating ratios of Class I railways (Brief, p. 22). This is a superficial suggestion. Of course operating ratios, representing the relation of total operating expenses (exclusive of taxes) to total operating revenues, fluctuate with the volume and type of total business. A railroad not operating at capacity can obviously carry additional business at a cheaper unit cost. This is true specifically of the Rio Grande. As Trustee Swan testified in 1942,

> ". . . . the higher the level of traffic the bigger the recovery on the additional business" (R. 1017).

This increase in profit, and resulting decline in operating ratio, is accentuated where the additional business, as is well known to have been the fact in recent war years, is in manufactured goods carrying higher rates, such as airplane engines, military equipment, chemicals, explosives, etc. It is all the more ominous that, in the face of such circumstances, the operating ratio of the Rio Grande increased from 57.4 in 1942 to 65.5 in 1943, though gross revenues were 16 million dollars greater,* and increased from 65.5 in 1943 to 70.7 in 1944 while total operating revenues remained substantially unchanged.** These trends confirm the liberality of the Commission's Plan.

3.

THE DEBTOR'S EXCURSIONS

We think there is no need here to follow the Debtor's excursions into the position of the stockholders in this case,† for the Debtor's petition for certiorari on those issues has not been granted, and we have no doubt the Court will allow a proper opportunity for briefs and argument were it ever to be allowed and the resulting issues presented. There is, of course, still less reason to pursue the Debtor's discussion of the position of stockholders in fourteen other railroad reorganizations, for they have never at any time been at issue in these cases. We think it sufficient here to record our disagreement with the views there urged. Since special emphasis is laid on the contention that interest should not be allowed at contract rates during the course of reorganiza-

*1943 Annual Report, pp. 11 and 19.

**"Income Account, Statement of Revenues, etc. for December 1944".

†Debtor's Brief, pp. 16-50 and Appendix A thereto.

tion, we might add that the contrary has been immemorially established, both as a "fixed principle" of reorganizations in equity,* and as to the rights of a secured creditor against his security in bankruptcy.** It has rightly been established also, by successive decisions of this Court, as a governing rule under the corporate reorganization laws, both in the case of industrials† and in the case of railroads.††

CONCLUSION

We respectfully submit that the orders of the Circuit Court should be reversed in their entirety, with instructions

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*American Iron and Steel Manufacturing Co. v. Seaboard Air Line R., 233 U. S. 261, 266-7 (1914); Ticonic National Bank v. Sprague, 303 U. S. 406, 412, 413 (1938).

**See *Louisville Joint Stock Land Bank v. Radford*, 295 U. S. 555, 597, n. 30 (1935); *Ticonic National Bank v. Sprague*, in next preceding footnote, and cases there cited.

†*Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510, 527 (1941).

††*Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R.*, 318 U. S. 523, 546 (1943); see *Ecker v. Western Pacific R. Corp.*, 318 U. S. 448, 509-10 (1943).

to affirm the orders of the District Court approving and confirming the Plan.

Dated March 1, 1946.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

Nos. 278, 279, 280, 281,
282, 286 and 291

IN THE MATTER

of

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY,

Debtor.

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, et al.,

Petitioners,

against

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, et al.,

Respondents.

(and the other six cases numbered above)

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF IN OPPOSITION

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August 31, 1945.

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The Plan, which gives the senior creditors "their claims in full" and, in addition, surplus cash on hand, earnings already accumulated and excess war profits, is inequitable and unfair to the General Mortgage Bondholders. Under Rule 38, this question is not one this Court should review 22

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IN THE

Supreme Court of the United States,

OCTOBER TERM, 1945

Nos. 278, 279, 280, 281, 282, 286 and 291

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RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, *et al.*,
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(and the other six cases numbered above)

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF IN OPPOSITION

Introductory

Three petitions for writs of certiorari have been filed, each asking this Court to review some part of a decision by the United States Circuit Court of Appeals for the Tenth Circuit entered on May 10, 1945. The decision involves a

proposed plan of reorganization (herein called the "Plan") of The Denver and Rio Grande Western Railroad Company (herein called "Debtor") under Section 77 of the Bankruptcy Act.

The petitions filed by the Debtor and by Guy A. Thompson, Trustee of Missouri Pacific Railroad Company (holder of half of Debtor's common stock) seek to have reviewed the part of the decision below which upheld the valuation of Debtor's property fixed by the Interstate Commerce Commission (herein called the "Commission"), and which held that the preferred and common stock of the Debtor are without value. The Court below affirmed the District Court on these matters.

The other certiorari petition was filed by Reconstruction Finance Corporation, Insurance Group Committee, and others. It seeks a review by this Court of that part of the decision below which, while accepting the valuation and framework of the Commission's Plan, held that the proposed treatment of the General Mortgage Bondholders was inequitable and unfair and that the rejection of the Plan by the General Mortgage Bondholders was reasonably justified within the meaning of the statute. On these questions the Circuit Court of Appeals reversed the District Court.

The Debtor's certiorari petition correctly urges that the Insurance Group petition is without merit and should be denied. The Debtor asks for a review of the matters covered by Debtor's petition only in the event this Court should grant the Insurance Group petition.

This brief will be limited to showing that the Insurance Group petition is without merit and should be denied. Unless otherwise indicated, all references herein (a) to the "petitioners" refer to the group consisting of the Reconstruction Finance Corporation, Insurance Group Committee, and others, and (b) to the "petition" refer to the petition dated July 31, 1945 filed by that group.

Opinions Below

The opinions of the Circuit Court of Appeals for the Tenth Circuit (R. 233-262)* and of the District Court (R. 187-206, 213-224) are not yet officially reported.

Questions Presented

1. Is a plan of reorganization which fails to provide for the distribution to creditors of the full amount of capitalization which the Commission found proper for the reorganized Debtor inequitable and unfair to junior creditors, who under the plan are receiving only 10% of their claim in new common stock, the remaining 90% of their claim being forever destroyed?

2. Is a plan of reorganization which awards to one class of senior creditors 100% of its claim in securities of the reorganized Debtor and also awards to that class of creditors all of the outstanding shares of the capital stock of another corporation, without determining the value of such capital stock, inequitable and unfair to junior creditors who have a junior lien upon such capital stock and who under the plan are receiving only 10% of their claim in securities of the reorganized Debtor and are having 90% of their claim wiped out?

3. Is a plan of reorganization which gives senior creditors their claims in full by awarding them 100% of their claim in securities of the reorganized Debtor and which, in addition, gives the senior creditors surplus cash on hand, earnings already accumulated and excess war profits inequitable and unfair to junior creditors, 90% of whose claim is to remain unsatisfied?

The Circuit Court of Appeals, in holding the Plan inequitable and unfair, determined the foregoing questions in favor of this respondent (R. 247-8, 250-1, 251-3). The decision of the Circuit Court of Appeals on these questions

* "R." refers to pages in abbreviated record printed pursuant to July 16, 1945 stipulation herein.

does not come within any of the classifications listed in paragraph 5 (b) of this Court's Rule 38. It is respectfully submitted that, if this Court were to review the decision below on the foregoing questions, it would reach the same result. Whether or not that is so, unless this case comes within one of the categories of Rule 38 (and it is respectfully submitted that it does not), the petitioners are not entitled to another appeal merely because this Court might not fully agree with the Court below or might have used different language in deciding certain of the questions.

Were the Court below to be reversed with respect to each aspect of the Plan which it considered and found inequitable and unfair, an additional question would be presented:

4. In the light of all the relevant facts contained in the voluminous record before the Circuit Court of Appeals, were the General Mortgage Bondholders reasonably justified in voting in May, 1944, by a four-to-one vote to reject the Plan?

The Circuit Court of Appeals ruled on this question 4, holding that the General Mortgage Bondholders "were reasonably justified, within the meaning of the statute, in rejecting the plan" (R. 253) and that, accordingly, the District Court erred in confirming the Plan in the face of their adverse vote (R. 253). This respondent submits that the Circuit Court of Appeals held correctly, but that the ruling was not necessary to the decision of the case because the Circuit Court of Appeals had already properly held the Plan inequitable and unfair. It seems too clear for argument that this is not the type of question that this Court should review, requiring as it does the consideration and weighing of *all* the evidence.

Were this Court to reverse the Court below on all of the questions already mentioned, even another question would be presented:

5. May Section 77 of the Bankruptcy Act properly be construed as giving the District Court power to confirm the Plan after 79.33% of the General Mortgage Bondholders

voting had rejected it; or is such construction an unwarranted and unconstitutional extension of the bankruptcy power?

This question 5 was raised below, but the Circuit Court of Appeals did not undertake to decide it. It clearly is not necessary for this Court to consider this last question unless this Court were to review, and to reverse, the Circuit Court of Appeals on all of the earlier questions.

The questions propounded by the petitioners

The petitioners, in stating what they conceive to be five questions which they believe this Court, under its Rule 38, should review on writ of certiorari, have misconstrued the opinion below in framing each of these questions and have made several errors. The questions which they assert should be here reviewed are not presented by the Circuit Court of Appeals decision.

The general question as stated by the Circuit Court of Appeals

After upholding the Commission's valuation of the Debtor's property for reorganization purposes, and affirming the District Court on this point, the Circuit Court of Appeals summed up the remaining problem as follows:

> "In considering whether the plan is fair and equitable, affords due consideration to the rights of each class of creditors, and whether it does not discriminate unfairly in favor of one class at the expense of another, *our problem is to determine whether within the framework of the capital structure set up by the Commission the assets have been distributed to the various classes of claimants within the rule of Northern Pac. Ry.* v. *Boyd*, 228 U. S. 482, and *Consolidated Products Co.* v. *DuBois*, 312 U. S. 510. These cases merely reiterate the well established equitable rule *that property of an insolvent corporation must be used to satisfy in full the claims of various classes of creditors according to their priority in rank*" (R. 246).*

* Unless otherwise indicated, all emphasis—by way of italicization or otherwise—is supplied.

The Circuit Court of Appeals held unanimously that, within the capitalization fixed by the Commission, that part of the Plan which proposed forever to wipe out 90% of the claim of the Debtor's General Mortgage Bondholders, is unfair and inequitable, and that the General Mortgage Bondholders were reasonably justified in rejecting the Plan by a vote of 4 to 1. This finding was based upon uncontroverted evidence showing that after all claims senior to the General Mortgage Bondholders were taken care of in full, there would remain within the valuation and capitalization fixed by the Commission securities available for distribution to the General Mortgage Bondholders of a par value substantially in excess of the $4,354,816, of stock allotted to them in the Plan. The Court left all adjustments for the Commission to make, expressly recognizing that claims of various classes of creditors must be taken care of "according to their priority in rank" (R. 246). The Court did not make, or suggest, any award of cash or new senior securities to the General Mortgage Bondholders, and petitioners' assertions to the contrary (petition 2, 3, 10, 12, 13, 15, 16) are erroneous.

The Statute Involved

The statute involved is Section 77 of the Bankruptcy Act (11 U. S. C. 205), particularly subsection (e).

STATEMENT

The Debtor's General Mortgage

This respondent, City Bank Farmers Trust Company, is the trustee of the Debtor's General Mortgage, under which $29,808,000, principal amount, of General Mortgage Bonds are outstanding (R. 37). The total General Mortgage claim as of the proposed effective date of the Plan, January 1, 1943, aggregated over 43½ million dollars (R. 183) and today amounts to almost 48 million dollars. The General Mortgage Bonds constitute almost one-fourth of

the Debtor's entire indebtedness and are the Debtor's junior bonds. The holders of the General Mortgage Bonds voted 79.33% to 20.67% (or about 4 to 1 of those voting) to reject the Plan (R. 266).

The Plan

The Plan under consideration is that embodied in the Interstate Commerce Commission's Third Supplemental Report and Order dated June 14, 1943, 254 ICC 349 (R. 151-186). The Plan is in the alternative, with or without consolidation with the Denver & Salt Lake. A summary of the Plan, without such consolidation, is given in Appendix B to the report (R. 183), a total capitalization of $143,528,027 being authorized (R. 159, 184). Throughout this brief, figures applicable to reorganization without such consolidation will be used consistently to avoid confusion.

The Plan is a drastic reorganization plan. Under it the General Mortgage Bondholders receive 10% of their claim in new common stock (being about 12% of the total new common stock). The remaining 90% of their claim is wiped out—that is, approximately 39 million dollars of their claim is forever cancelled. The Plan also wipes out (a) the Debtor's unsecured indebtedness aggregating about 440 thousand dollars, (b) the Debtor's preferred stock outstanding in the amount of 16½ million dollars, and (c) the Debtor's 300,000 shares of common stock, carried on the balance sheet at about 62½ million dollars. All in all, the Plan eliminates claims aggregating, as of the proposed effective date, over $118,300,000 (R. 36-7, 183).

Because of developments since the Plan was proposed by the Commission, were the Plan now to be put into operation, the capitalization of the reorganized Debtor would *not* be 143½ million dollars, the amount authorized by the Commission, but something less than 140 million dollars—notwithstanding the fact that in the meantime the value and earning capacity of the property have been substantially increased and the net working capital position has been greatly improved. The elimination of 3½ million dollars, or more, from the already drastically reduced capitalization

authorized by the Plan would be a serious injustice to the General Mortgage Bondholders.

The senior creditors

The Commission and the District Court have found in effect, and the Circuit Court of Appeals has agreed (R. 247, 251), that the claims of all creditors senior to the General Mortgage Bondholders were satisfied in full by the treatment proposed for such creditors in the Plan. Obviously that must be so if there was anything at all left over for distribution to the General Mortgage Bondholders. All of the plans at any time proposed for the Debtor have provided new securities for the General Mortgage Bondholders—100% of their claim in new preferred or common stock in the first plans, 10% in the present Plan (R. 350). The three plans proposed by the senior security holders during the course of the reorganization proceedings gave the General Mortgage Bondholders a maximum of 100% and a minimum of 47.42% of their claim in new stock (R. 350).

By their conduct throughout, the senior creditors have acquiesced in the proposition that some "value" for reorganization purposes is available for distribution to the General Mortgage issue. They support this present Plan. They supported it when it came before the District Court for approval in September, 1943. Moreover, when the earlier plans were proposed, they never urged that any of them treated the General Mortgage Bondholders too favorably. As a matter of fact, an examination of the record discloses that whenever the Commission or its examiner proposed a plan, the senior security holders, in their *very next* plan, proposed that *better* treatment be accorded the General Mortgage issue (R. 350).

History

Circuit Judge Phillips in his concurring opinion summarized pertinent features of the Plan and its history as follows:

> "On November 1, 1935, during the depths of the national depression, the debtor came into court for

reorganization. At that time the debtor's senior debts ahead of the general mortgage bonds aggregated slightly over $101,000,000 and the claim of the general mortgage bondholders aggregated about $30,000,000. With an immediate reorganization, a capitalization of $132,000,000 would have been adequate to give the general mortgage bondholders new stock equal to 100 per cent of their claim. *No capitalization or valuation ever proposed for the debtor, in any plan presented, has been that low.* During the eight years' delay in reorganization (in nowise due to the general mortgage bondholders, but, at least in part, to controversies among the senior security holders) and up to January 1, 1943, the effective date of the plan, the claims of the senior security holders, due to the accrual and nonpayment of interest, increased about $38,000,000. The debtor's net income available for interest during the trusteeship to the end of 1944 amounted to $49,420,972. *It exceeded by approximately $9,500,000 the interest charges which accrued on the claims of senior security holders to the end of that year.* As of December 31, 1935, the debtor's current assets were $9,727,230 less than its current liabilities. As of December 31, 1944, the debtor's current assets exceeded its current liabilities by $12,125,863.50. *Thus, it will be seen there has been a favorable change in the current situation of $21,853,093,* and, moreover, since the plan was formulated, the Junction Bonds have been paid and equipment obligations have been reduced from $5,758,000, the amount provided for in the plan, to $4,540,000, a reduction in that requirement of $1,218,000.

"Approximately $43,000,000 of the income available, but not used, for the payment of interest has been expended in permanent improvements and betterments. While the investment value of the debtor's property thus was substantially increased, the Commission's valuation, based on estimated future earnings, was not increased proportionately. As a result, the claim of the senior security holders has increased and the participation of the general mortgage bondholders has been pressed downward until it is now fixed at 10 per cent of the new common stock. Many of the improvements and betterments referred to

above, have substantially increased the capacity of the railroad to handle increased traffic as it arises * * *" (R. 256-8).

The situation is similarly summed up by Circuit Judge Huxman, in the Court's opinion, in which Circuit Judges Phillips and Murrah both concurred (R. 248-9).

Notwithstanding these facts, Judge Phillips felt constrained to hold:

> "The broad language of the Supreme Court in the Western Pacific case and the Milwaukee case compels me to conclude that we cannot disturb the Commission's finding of valuation * * *." (R. 254)

The Court's opinion by Judge Huxman, in which all concurred, held similarly:

> "It is settled beyond the question of a doubt by the decisions of the Supreme Court in Ecker *v.* Western Pac. R. Co., and Group of Investors *v.* Milwaukee R. Co., supra, and in the special concurring opinions of Justice Roberts in those cases, that the duty of formulating a plan of reorganization under Section 77, including the adoption of a new valuation of the property, is a function confided to the Interstate Commerce Commission, and that no court of law may interfere with such plan or valuation because it does not agree with it. * * * Courts may interfere with the capital structure or valuation made by the Commission in a proceeding under this Act only when it can be said as a matter of law that the Commission used fundamentally erroneous methods of valuation or acted arbitrarily or capriciously. An examination of the entire record leads to the conclusion that the action and the conduct of the Commission in fixing the valuation and setting up the capital structure is free from these infirmities, and that its action in relation thereto must be upheld." (R. 244-5)

There is no basis for the assertions in the petition that the Court below failed to follow the decisions of this Court.

Earnings

The statements in the petition relative to the Debtor's earnings are incomplete and misleading. The Debtor's earnings record has been good except for the depression years. In the six years preceding the depression, 1925 to 1930, inclusive, the Debtor's net income available for interest ranged between 6½ and 8¾ million dollars annually (R. 348). Since the end of 1941 (and the making of a substantial part of the investment of 43 million dollars in permanent improvements, mentioned in Judge Phillips' opinion), the Debtor's net available for interest has been running between 10 and 17 million dollars annually (R. 280-1; 348, 349). There is undisputed testimony in the record that the improvements can be expected to yield a return of 10 to 15 per cent or even more (R. 316-7). That would indicate an increase in earnings, resulting from the improvements, of between 4 and 6½ million dollars a year. There have been some property retirements, but unchallenged testimony is in the record that these abandonments and retirements have *improved* the earning capacity of the road (R. 332) and hence *increased* its value for reorganization purposes.

The Debtor's annual interest requirements for all old securities senior to the General Mortgage Bonds total less than 4½ million dollars (R. 349; col. III). The annual interest charges on the General Mortgage Bonds amount to about 1½ million dollars.

From the institution of these reorganization proceedings in 1935 up to the end of 1944 the Debtor's income available for interest has totalled approximately 50 million dollars (R. 349; col. II), and the total interest requirements for all creditors' claims senior to the General Mortgage Bonds have amounted to about 40 million dollars (R. 349; col. III), leaving a total of about $9,779,000—or an average of over one million dollars a year—of earnings available for the General Mortgage issue (R. 349; col. IV), being approximately two-thirds of the contract interest requirements of that issue. This period includes the five worst years in the present company's history (R. 348).

The Junction Bonds and the surplus cash

Of the 143½ million dollar capitalization authorized in the Plan, about 2¾ million dollars of new senior securities were to be issued in exchange for the Junction Bonds (the First Mortgage Five Per Cent Bonds of The Rio Grande Junction Railroad Company, a wholly-owned subsidiary of the Debtor, owning that part of Debtor's main line from Rifle to Grand Junction, Colorado.)

Some nine months after the proposed effective date of the Plan, the District Court directed that the Junction Bonds be paid or purchased from excess cash on hand (R. 262-3, 264-5), saying:

> "The Court: * * * *This railroad has an amount of cash here that it is not necessary to carry forward into the reorganization; it is not necessary for the proper financing of the new company, and even if this two million dollars plus is paid, there would still be plenty of working capital to go ahead with, under the plan.*
>
> "I have old-fashioned ideas, perhaps, and in all receiverships in this court, where there are debts and assets to pay them, I believe in paying off one's debts; that that is the best financing there is. * * *
>
> "So the order of the Court will be that these Rio Grande Junction Bonds be paid, with interest * * *
>
> "Mr. Gibson: If the Court please, with that ruling and order, may I ask your Honor whether you would consider reaching that result by way of purchase rather than a payment, in order to avoid serious income taxes?
>
> "The Court: Yes, you may make the order in any way so that it will avoid taxes or most convenient in considering these incidental questions that may arise * * *" (R. 262-3).

By the application of "surplus cash" (R. 262, 263), the first lien upon the Junction property, amounting to approximately 2¾ million dollars, has been eliminated—without the necessity of issuing the 2¾ million dollars of authorized Plan securities which the Commission had allocated to that particular purpose. After the application

of this surplus cash, more cash and "net current working capital" remained than were on hand at the time the Plan was promulgated (R. 278, 298). The system earning capacity has been in no wise decreased by the use of "surplus cash". If there has been no lessening of the earning capacity, there is no justification for any decrease in the total authorized capitalization. If the 2¾ million dollars of authorized securities were not "redistributed", as prayed by this respondent and as the Circuit Court of Appeals indicates should be done (R. 250-1), the net result would be that the authorized capitalization of the reorganized company would be *decreased* by that amount—although there would be no corresponding decrease in its earning capacity.

There is a precedent for such a "redistribution" of securities in this very case. The Commission's July 27, 1942 report and order reserved 2¼ million dollars of the authorized capitalization for possible new-money requirements (R. 121, 124, 145, 353). By the time that report and order reached the parties for their consideration, it seemed clear that the 2¼ million dollars of authorized capitalization reserved for new-money requirements was unnecessary and that accordingly, within the capital structure authorized by the Commission, that amount of capitalization had become available for redistribution. The Commission therefore "redistributed" the securities which had been reserved to cover new-money requirements (R. 161-2).

In similar situations in the *Milwaukee*[1], and *New Haven*[2] cases (reviewed later; this brief 31-33, 27-31), the plan securities allotted to the claims subsequently paid in cash were, upon such payment, redistributed to the other creditors—so that the total authorized capitalization was not

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[1] *Chicago, Milwaukee, St. Paul & Pacific Railroad Company Reorganization* (1943), 254 I. C. C. 707; 257 I. C. C. 223; (7th C. C. A. 1944) 145 Fed. 2d 299; certiorari denied (1945) —— U. S. ——, 65 Sup. Ct. 860, 89 L. Ed. 687.

[2] *In re New York, New Haven & Hartford R. Co.* (D. C. D. Conn. 1943), 54 Fed. Supp. 595; (1944), 257 I. C. C. 9; (2nd C. C. A. 1945), 147 Fed. 2d 40; certiorari denied (1945) —— U. S. ——, 65 Sup. Ct. 1578, 89 L. Ed. 1353.

thereby decreased. The General Mortgage Trustee applied for such a redistribution in the *Denver* case, but the District Court denied the application. The General Mortgage Trustee appealed from that order as well as from the order confirming the Plan.

The Circuit Court of Appeals reversed that part of the District Court's ruling, saying in part:

> "The Junction Bonds
>
> "We think that the complaint as to the manner in which the Junction Bonds were handled is well taken. The Rio Grande Junction Railroad is a wholly owned subsidiary of the Debtor. It had bonds outstanding in the hands of the public for the payment of which the Debtor was liable, totaling $2,758,333. This claim was senior to that of the General Bondholders. The plan set aside securities for the payment of this claim. In an order dated September 13, 1943, the District Court directed the trustee to pay this claim with some of the surplus cash on hand * * * The fact remains that the new capitalization provided securities for the payment of these bonds. * * * When surplus cash was used to pay this claim, the value behind the securities set aside for that purpose remained undistributed. * * * this undistributed value in all equity and fairness belonged to the General Bondholders. Any plan which does not give it to them does not comply with the requirements of Section 77(e) of the Act." (R. 250-1).

The Circuit Court of Appeals recognized that the redistribution would be made to the "various classes of creditors according to their priority in rank" (R. 246), holding:

> "* * * We think the interests of all parties can best be served by having the entire matter [including, of course, the equitable redistribution of the value represented by the undistributed securities]* reconsidered by the Commission and have it make all necessary adjustments." (R. 253).

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*Material enclosed by brackets, appearing in quotations, has been inserted by way of explanation.

Any competent accountant on the Commission's staff can work out such a redistribution so as to maintain the priority in rank of all classes of creditors established by the Commission. When such redistribution is accomplished, then, after all senior claims are paid in full either in cash or new securities or both, there will of course be left over within the valuation and capitalization fixed by the Commission new common stock available to the junior General Mortgage Bondholders in excess of the 10% of their claim originally provided for in the Plan.

It perhaps should be made clear at this point that this respondent at no time has made any claim that the General Mortgage Bondholders should receive cash or senior securities "released" through the payment or purchase of the Junction Bonds. A fair reading of the opinion below fails to disclose *any* requirement or direction by the Circuit Court of Appeals that any cash or new senior securities should be "awarded" or "allocated" to the General Mortgage issue. Statements to that effect (petition 2, 3, 10, 12, 13, 15, 16) are not correct.

The Circuit Court of Appeals pointed out that inasmuch as the senior bondholders had been satisfied in full (R. 247, 251; this brief 8), this "undistributed value" (i. e. 2¾ million dollars of the *authorized new capitalization—not* the senior securities released), in all equity and fairness belongs to the General Mortgage Bondholders (R. 251). The Commission has given the Debtor's property a "value" for reorganization purposes of 143½ million dollars. The Circuit Court of Appeals clearly was referring to part of this, the Commission's *value* for reorganization purposes, when it spoke of "this undistributed value" which "in all equity and fairness belonged to the General Bondholders" (R. 251).

Similarly, it was "value" for reorganization purposes which the Circuit Court of Appeals had in mind when it said, with respect to the decrease in other senior debt: "It would be inequitable to give this additional *value* to the Senior Bondholders when they have already been fully

compensated" (R. 251). The Circuit Court of Appeals agreed with this respondent that, in view of the great severity of the Plan in its proposed treatment of the General Mortgage issue, no further reduction in the authorized capitalization should be permitted and the General Mortgage Bondholders should be given the benefit of every available part of the authorized capitalization not required for the satisfaction of the claims senior to the General Mortgage issue.

The suggested "exclusion" of the Junction Bonds

Before leaving the question of the Junction Bonds, one other error in the petition should be corrected. The petitioners argue that the Commission "construed" the District Court's action in directing the purchase or payment of the Junction Bonds as an exercise of a reserved power to "exclude" the Junction Company (petition 7-8). That is clearly wrong. The Plan provided that, if the consolidation of the Junction presented difficulties which might delay consummation, the provisions for the holders of the Junction Bonds might be considered wholly separable (R. 166); but there has been no such finding, and no evidence has been introduced to that effect. Furthermore, it would have been improper for the Commission so to construe the District Court's action. If the Junction bondholders had been "excluded" from the Plan, there would remain *outstanding* a lien upon the Junction property in the hands of third persons. Through its stock ownership, the reorganized Debtor would have the Junction property, but subject to this outstanding 2¾ million-dollar lien. That is not our case. The Junction Bonds have not been excluded; they have been acquired or paid off—with cash accumulated after the Commission promulgated the Plan, which the District Court has several times described as "surplus cash" (R. 262, 263) not required for any of the purposes of the reorganization (R. 262).

The Utah Fuel stock

The statements in the petition in regard to the Utah Fuel stock, are erroneous and incomplete both as to the facts and the questions presented.

The Rio Grande Western Railway Company (a predecessor of the Debtor), in 1901 bought all the stock of Utah Fuel Company for $6,000,000 and paid for the stock by putting the stock under the Western Consolidated Mortgage (one of those senior to the General Mortgage) and issuing $6,000,000 of Western Consolidated Bonds to the former owner of the stock.

As of December 20, 1924, pursuant to a plan of reorganization, the Debtor entered into an agreement whereby the Utah Fuel stock was transferred to James S. Alexander, as trustee, still subject, however, to the lien of the Western Consolidated Mortgage, and it was provided that the income from the stock should be paid to the Debtor as long as any of the Debtor's General Mortgage Bonds or Refunding Mortgage Bonds should remain outstanding. Paragraph Fifth of the agreement provided that in the event of the foreclosure of the General Mortgage, the trustee under that agreement, upon the demand of this respondent, the General Mortgage Trustee, should sell the pledged Utah Fuel stock, still subject to the Western Consolidated Mortgage, the net proceeds to be applied to the payment of the General Mortgage Bonds and Refunding Mortgage Bonds, in accordance with the relative priority of lien of such mortgages—all pursuant to the directions and supervision of the court in charge of such foreclosure proceedings. By another agreement bearing the same date the Debtor assigned to this respondent, the General Mortgage Trustee, and to the trustee of the Refunding Mortgage all of the Debtor's rights and interests "in, to and under" the first agreement of December 20, 1924. Thus, in effect, this respondent has had since December 20, 1924, a junior lien upon the pledged Utah Fuel stock. (Transcript C. C. A. case Nos. 2906-7, Vol. 7, page 3171 et seq.) Title to the Utah Fuel stock was placed in a trustee to accomplish the purposes above described, but the real beneficial ownership

of the stock at all times has belonged to the Debtor herein and its creditors, including the General Mortgage Bondholders. Neither the Western Pacific nor the Missouri Pacific have any equity rights in the stock as long as the General Mortgage Bonds remain unpaid. Upon satisfaction of the Western Consolidated Bondholders' claim in full, the junior lienors are entitled to the benefit of this collateral.

Despite this fact background, the petitioners argue that "The Debtor does not own the Utah Fuel stock and never has", that this stock "is not the property of the Debtor" (petition 6, 21) and that accordingly the Western Consolidated Bondholders are entitled to retain the benefit of this stock *in addition* to receiving securities of the reorganized Debtor in the full face-amount of their claim. They cite as authority a case in which there was no junior lien on the collateral and accordingly not applicable here.

The Plan, after providing for the payment in full of the claim of the Western Consolidated Bondholders by the issuance of $20,056,400 in new securities of the reorganized Debtor, proposed, in addition thereto, to award to these creditors *all* the stock of the Utah Fuel Company, reputedly worth today between 4½ and 20 million dollars.

The Circuit Court of Appeals said, in part, with regard to this Utah Fuel stock:

> "There can be no question as to the duty resting upon these claimants [the Western Consolidated Bondholders] to credit the value of this collateral [the Utah Fuel stock] upon their claim before sharing in the securities of the reorganized company. They were entitled only to full payment. If the new securities which were assigned to them satisfied their claim in full, then the plan which permitted them to retain in addition this collateral would be inequitable and unfair to junior creditors.
>
> "The findings of the Commission are not clear as to the manner in which it treated this collateral. * * *
>
> "*Neither does the record establish with any degree of satisfaction the value of this collateral.* There is evidence which would support a conclusion that it had but little value. On the other hand, there

is evidence that the Utah Fuel Company is now prosperous and is enjoying large earnings, with reasonable prospects that they will continue.

"It appears to us that the plan contemplates that the claim of these creditors was to be *satisfied* from the new securities which were set apart for them, and that no particular value was ascribed to this collateral. If this collateral has any substantial value, it must be taken into account before the amount of new securities which are to be set over to these claimants is determined. *The Commission should clear up the doubts and uncertainties which surround this matter* when the proceedings are returned to it for further consideration" (R. 252-3).

The only question decided by the Circuit Court of Appeals relating to the Utah Fuel stock was that it could not properly decide upon the fairness of that part of the Plan dealing with the stock without knowing whether or not the Commission had determined the value of the stock, what that value is and whether or not the Commission intended to give it as a "bonus" to the Western Consolidated issue.

The Utah Fuel Company is an operating coal company owning lands containing estimated reserves of about 115,000,000 tons of coal, mining about 2,000,000 tons of coal per year, with gross operating revenues of about $6,000,000, and a substantial net income. The value of the Utah Fuel stock may today be between $15,000,000 and $20,000,000. The Commission's first report, back in the depths of the depression (R. 52), states that the Utah Fuel Company's balance sheet of December 31, 1936, shows the asset value of the Utah Fuel Company then to be over $15,000,000, the par value of the stock to be $10,000,000, with a 1936 corporate surplus of over 2½ million dollars—even in the depression. The Commission in its earliest report refers to a 1936 depression-year appraisal of the Company by someone employed by Guaranty Trust Company indicating a value of only $4,653,720. This low figure was reached by writing down the land value (land containing 115,000,000 tons of coal and now producing 2,000,000 tons annually) from about $10,000,000 to about $2,000,000 (Transcript C.C.A. Cases Nos. 2906-7, Vol. 9, pp. 4169-4282):

ARGUMENT

Question 1*

The Plan, which fails to provide for the distribution of the entire capitalization which the Commission found proper for the reorganized Debtor, is inequitable and unfair to the General Mortgage Bondholders. Under Rule 38, this question is not one this Court should review.

Under the decisions of this Court in the *Milwaukee*[1] and *Western Pacific*[2] cases, the determination of the proper amount of the capitalization of the reorganized Debtor is the function of the Commission. The Commission has found that without consolidation with the Denver & Salt Lake "there will be adequate coverage of fixed charges of the new company" and that the "value" of the property "for the purposes of this proceeding * * * is approximately $143,528,027" (R. 159). The Commission's Plan accordingly authorizes securities of the reorganized Debtor totalling that amount (R. 184).

Of those authorized, approximately 2¾ million dollars of senior-grade securities were intended for the purpose of taking care of the Junction Bonds (R. 183). They will not be required for that purpose, because the District Court has directed that "surplus cash" be used for their acquisition (R. 262, 263) and substantially all of them have been so acquired (R. 277-8).

The District Court nevertheless held that the Plan did not permit the redistribution of these securities, saying that "such a reallocation of securities can only be made by the Commission" (R. 223). Accordingly, with the Plan so interpreted, the actual capitalization of the reorganized Debtor is *reduced* by this amount of 2¾ million dollars below the

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*This brief page 3.

[1] *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul & Pacific Railroad Co.* (1943) 318 U. S. 523, 63 Sup. Ct. 727, 87 L. Ed. 959.

[2] *Ecker* v. *Western Pacific Railroad Corp.* (1945) 318 U. S. 448, 63 Sup. Ct. 692, 87 L. Ed. 892.

total fixed by the Commission, although the system has *all* of the assets and earning capacity contemplated by the Commission (this brief 12-16).

An additional $1,218,000 of the authorized capitalization represented debts due other senior creditors which have, since the Plan's promulgation, been paid in cash. As the Plan has been interpreted, this part of the authorized capitalization would also remain unissued and the actual capitalization would be reduced accordingly (R. 251).

The Circuit Court of Appeals has held that because of the foregoing the Plan "does not comply with the requirements of Section 77(e) of the Act" (R. 251). Obviously that must be so. No question is presented by that ruling which calls for the exercise of this Court's power of review.

Question 2*

The Plan, which gives senior creditors a "bonus" of 100,000 shares of Utah Fuel stock, without determining the value of that stock, is inequitable and unfair to the General Mortgage Bondholders, who have a junior lien on that stock. Under Rule 38, this question is not one this Court should review.

The Plan provides that the holders of the Western Consolidated Bonds shall receive 100% of their 20-million-dollar claim in new securities of the reorganized Debtor (R. 183). It also provides that these creditors shall receive all of the pledged Utah Fuel stock (R. 167). The Circuit Court of Appeals says that it "appears to us that the plan contemplates that the claim of these creditors [the Western Consolidated bondholders] was to be *satisfied* from the new securities [the securities of the reorganized Debtor] which were set apart for them, and that no particular value was ascribed to this collateral [the Utah Fuel stock]" (R. 253). That is a fair inference from the Plan language.

The Circuit Court of Appeals has held that the record does *not* "establish with any degree of satisfaction the value of this collateral" (R. 253). That decision is not a question of the type this Court should review under its Rule 38.

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*This brief page 3.

The General Mortgage Bondholders, who are to receive only 10% of their claim under the Plan (R. 183), have a junior lien on the Utah Fuel stock (this brief 17-8), and are entitled to share in the benefit after senior lienors have been satisfied.

The Circuit Court of Appeals has held that the "Commission should clear up the doubts and uncertainties which surround this matter" (R. 253). It is respectfully submitted that it would be impossible intelligently to pass upon the fairness and equity of the Plan without some determination as to the value of the Utah Fuel stock, upon which this respondent has a junior lien and which under the Plan is turned over to some of the senior creditors, with no duty upon them to account to the General Mortgage Bondholders. The instructions of the Circuit Court of Appeals are required by every consideration of fairness and do not present any question for the exercise of this Court's review power.

Question 3*

The Plan, which gives the senior creditors "their claims in full" and, in addition, surplus cash on hand, earnings already accumulated and excess war profits, is inequitable and unfair to the General Mortgage Bondholders. Under Rule 38, this question is not one this Court should review.

The Circuit Court of Appeals recognized that under the applicable decisions of this Court it could not itself increase the valuation fixed by the Commission, however much it might disagree with the Commission's conclusions—always provided that the Commission had not used "erroneous methods" of valuation (R. 244-5, 254). It also recognized that war earnings may be "disregarded in setting up the capitalized structure" for the reorganized Debtor (R. 247). It questioned, however, the propriety of disregarding entirely net earnings *already accumulated* as a result of swollen war earnings (R. 247) and said that a plan which gives the senior bondholders (a) "*their claims in full* by substan-

*This brief page 3.

tially delivering the road to them", and, in addition, (b) "the surplus cash actually on hand" and (c) "the excess war profits which are reasonably sure to come" is "*inherently inequitable and unfair*" as long as there are creditors whose claims are not fully satisfied (R. 247).

The senior creditors under the Plan are to receive about 97% of the securities of the reorganized Debtor. Thus, as the Court below says, the road is substantially "handed over" to them (R. 249). The General Mortgage issue, constituting almost one-fourth of the Debtor's outstanding indebtedness, is to receive the remaining 3% of the new capitalization. After pointing out that more than $43,000,000 of net earnings accumulated during the reorganization had been invested "in building a new railroad in many respects" (R. 249), the Court below admitted that the Commission was not compelled to add the "amount of these expenditures to the capitalized value" (R. 249), but the Court below indicated that the failure to do so accentuated an "inherent weakness" of the Plan in failing to make "equitable distribution of the excess current assets on hand" and the excess war profits (R. 248, 249). The Court below in this respect is in accord with the decisions in the *New Haven*, *Milwaukee*, *Florida East Coast* and *Missouri Pacific* cases hereinafter discussed (this brief 28-35).

It further said that there is "*more* than a speculative probability" that (a) the "war industries which have been constructed along the system" and (b) the "improvements which have been made by the use of these net earnings", together, may "produce greater net returns than anticipated in the plan" (R. 250) and it "suggested" a method by which the Commission could protect the interests of the General Mortgage Bondholders.

In doing this, it seems too clear for argument that the Circuit Court of Appeals has not required any "substantial change" in the capital structure by "adding additional new junior securities" or "additional new securities apparently of senior grades" (petition 2, 3, 19). The petitioners have misconstrued the Circuit Court of Appeals. The Circuit Court of Appeals "suggested", by way of remedy:

"*It could be done* by issuing to the General Bondholders an additional amount of a subordinate stock which would receive returns only from excess dividends" (R. 250). The Court, however, continued *immediately, in its very next sentence* as follows: "*This is a mere suggestion on our part, in no wise binding on the Commission.* Our duty is limited to pointing out defects in the plan. It is the responsibility of the Commission to correct them" (R. 250). Thus, the Court below has *not* held that "substantial changes" in the capital structure must be made or that "additional new securities" must be issued. There are many other ways of accomplishing the indicated correction. The Circuit Court of Appeals has made a suggestion; it has taken great care to say that it is only a "suggestion" and not "binding" on the Commission.

Question 4*

The General Mortgage Bondholders were reasonably justified in rejecting the Plan. Under Rule 38, this question is not one this Court should review.

Questions 4 and 5 have to do with the so-called "cram-down" provision of Section 77(e). Neither of them need now be considered by this Court unless this Court were first to determine that the Circuit Court of Appeals was wrong about the Junction Bonds question, about the situation presented by the decrease in other senior indebtedness, about the Utah Fuel stock, about the equitable distribution of accumulated earnings, in fact about every question having to do with the inequity and unfairness of the Plan.

The petitioners have made an error in stating that the Circuit Court of Appeals has ruled that "the dissent of the General Mortgage bondholders precluded confirmation of the Plan" (petition 23). An examination of the opinion will show that it contains no such holding. The Circuit Court of Appeals pointed out numerous respects in which it found that the Plan was *inequitable* and *unfair* and *did not comply*

*This brief page 4.

with the requirements of Section 77(c) and *then* held: "It follows from what has been said that the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, * * *" (R. 253). The Court decided, first, that because the Plan was not fair and equitable, the rejection vote was reasonably justified; and, secondly, that, because the Plan was not fair and equitable *and* because the rejection vote was reasonably justified, the District Court erred in confirming the plan (R. 253). That is very far removed indeed from the assertion that a rejection vote "precludes" confirmation.

The position of the petitioners on the cram-down provision seems to be that Section 77(c) does not mean what it says, that the provision for submitting a plan of reorganization to creditors for a vote is meaningless, that no creditor can be "reasonably justified" in voting to reject a plan once the District Court has found it "fair and equitable" (which the District Court under the statute is required to find *before* any plan can be *submitted* to security holders for a vote). If the petitioners were right about this, it would mean that everything prescribed in Section 77 as the procedure to be followed after an "approval" order is a futile waste of time and money—that the Congress was imposing meaningless procedural red tape in providing so carefully for the submission to creditors and that the Commission was merely shadow boxing in conducting, tabulating and reporting with such meticulous care the vote of each class of creditors.

This respondent respectfully submits that such cannot be presumed to have been the intent of Congress. The statute means just what it says. After a rejection vote, the Court may not confirm the plan—cram it down the throats of the class of creditors which rejected it—unless the Court properly finds, on the basis of competent and convincing evidence, that the rejection was not reasonably justified in the light of the relevant facts—that those who voted to reject acted from some improper motives, or were arbitrary or capricious in their action. No evidence to

that effect was offered. It would be impossible, it would seem, to show that the rejection vote was unreasonable when the unanimous Circuit Court of Appeals found that the Plan was "inherently inequitable and unfair" (R. 247) and "fails to meet the requirements of Section 77(e) * * *" (R. 251, 253). If anything more were needed, it is obvious that the unanimous House Judiciary Committee felt the same way about the Plan—as can be seen from the extracts from a committee report which appears as a footnote to the opinion of Judge Phillips (R. 255-9). Unless all three Judges of the Circuit Court of Appeals for the Tenth Circuit and all members of the House Judiciary Committee were unreasonable, it would seem impossible to hold that the rejection vote was not reasonably justified.

But this Court cannot review the decision below that the rejection was "reasonably justified, within the meaning of the statute," i. e. "in the light of * * * all the relevant facts" (Section 77(e)), without reviewing all of the voluminous record before the Circuit Court of Appeals. Whether or not this Court might have reached a different conclusion (and this respondent submits it would not) this is not the type of question this Court, under its Rule 38, should review on certiorari.

Question 5*

The constitutional question is not now presented.

The constitutionality of Section 77 was sustained by this Court in the *Rock Island*[1] case by an analogy to compositions. About five months *after* the decision of this Court in the *Rock Island* case, the statute was amended by the addition of the cram-down provision in its present form. If that provision is interpreted to mean that the District Court may, under the circumstances specified, confirm a plan in the absence of the statutory two-thirds vote of ap-

*This brief pages 4-5.

[1] *Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Railway Co.* (1935), 294 U. S. 648, 667-75, 55 Sup. Ct. 595, 79 L. Ed. 1110.

proval provided that at least a *majority* vote of approval is obtained, then the amended statute may be sustained on the basis of the *Rock Island* case reasoning. But, if the cram-down section were interpreted to mean that the District Court may confirm a plan in the *absence* of even a *majority* vote of approval, then it would be necessary to find some other basis upon which to sustain the constitutionality of the statute. The reasoning upon which this Court relied in the *Rock Island* case would no longer be applicable.

In the *Radford*[1] case, in holding the Frazier-Lemke Act unconstitutional, this Court said:

> "* * * In no case of composition is a secured claim affected except when the holder is a member of a class; and then *only when the composition is desired by the requisite majority and is approved by the court.* * * *." (295 U. S. 585-6).
>
> "* * * The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment. * * *" (p. 589).

In discussing the power of the bankruptcy court to enforce a composition between creditors, this Court further observed:

> "* * * It is the same power which a court of equity exercises when it compels dissenting creditors, in effect, to submit to a plan of reorganization approved by it as beneficial and assented to by the requisite *majority* of the creditors. * * *" (p. 585).

But, unless this Court were first to conclude that it should (1) review and (2) reverse the Circuit Court of Appeals on each of questions 1 to 4, inclusive, this constitutional question is not now presented for consideration.

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[1] *Louisville Joint Stock Land Bank* v. *Radford* (1935), 295 U. S. 555, 55 Sup. Ct. 854, 79 L. Ed. 1593.

The opinion below is in accordance with the decisions in other circuits.

The New Haven case (2d Cir.)

A "redistribution" of part of the authorized capitalization, similar to that suggested in our *Denver* case, was made in the *New Haven*[1] reorganization where about $26,000,000 of surplus cash was used to reduce senior claims after the New Haven plan came out.

Judge Hincks, in discussing the first 18 million dollars of cash used in reducing these senior claims in the *New Haven* case, said in part:

> "* * * As a result of these * * * payments the aggregate amount of the secured claims has been reduced and if new securities were now to be used * * * for the discharge of the old [unpaid] securities there would be needed * * * [18 million less of new securities]. *This would produce a capital structure in which the bonded indebtedness was less than that which in the judgment of the Commission the enterprise could reasonably be expected to support. Thus a block of $6,599,290 in fixed interest bonds and $11,658,890 in income bonds became available to sweeten the treatment previously proposed for all mortgage creditors who had not already received an allotment * * * equal to the amount of their claims.* * * *

> the Commission * * *. These relationships can be established by mathematical computations based solely upon findings of the values of the several issues already made by the Commission * * *." (p. 608)

Pursuant to this decision, the Commission on February 8, 1944[1] worked out the redistribution of the released securities, saying in part:

> "Consistently * * * in accordance with the Court's interpretation, the plan should also be corrected to provide that, *if*, pending reorganization, any future *payment * * * shall reduce or eliminate the claim of a secured creditor or of a class of secured creditors, the excess new fixed interest or new contingent interest bonds allocated to such creditor or class of creditors * * * thus released and becoming available shall be redistributed under the method used in the formulation of appendix A * * * *" (257 I. C. C. 11).
>
> "*Accordingly * * * if the claims are so paid, the securities allocated to the banks under the plan will be distributed to other secured creditors.* * * *" (257 I. C. C. 13).

Altogether about $26,000,000 cash accumulating after the Plan came out was used in the *New Haven* case to reduce senior claims and the new securities thereby released were redistributed.

The District Court in our *Denver* case denied this respondent's petition for a similar redistribution of the securities released by the payment or purchase of the Junction Bonds, although apparently it may not have fully agreed with the treatment accorded the General Mortgage issue. For example, in the confirmation order Judge Symes said:

> "The court in its plan of March 6, 1941, gave the General Mortgage bondholders more common stock than does the approved plan. The Commission, how-

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[1] *New York, New Haven & Hartford Railroad Reorganization, Finance Docket 10992*, fifth supplemental report, dated February , 1944, 257 I. C. C. 9.

ever, could not agree with our views, and it would seem to be a useless gesture for the court to make the same error again, assuming we had the power" (R. 221).

This respondent having pointed to the New Haven precedent, the Court, in refusing to follow it, said:

> "Frankly, I do not believe the court has the power to make the reallocation requested by the General Mortgage trustee * * *" (R. 217).
>
> "* * * *the action of Judge Hincks is hardly authority—at least until approved by an appellate court.* * * *" (R. 216).

Thereafter, however, the Circuit Court of Appeals, Second Circuit,[1] upheld Judge Hincks' decision on this redistribution matter and also upon the procedure followed by the New Haven court, saying:

> "* * *. We regard it as a commendable instance of 'properly coordinated action' between the Court and the Commission, the importance of which was noted in Ecker v. Western Pacific R. Corp., 318 U. S. 448, 475; 63 S. Ct. 692, 708; 87 L. Ed. 892." (147 Fed. 2d 44-5).

In the *New Haven* case the Circuit Court of Appeals reversed the District Court decision on another point, ordering a further adjustment within the framework of the Commission's plan, because of inequitable treatment of one class of creditors, and petitions for writs of certiorari were denied June 18, 1945.[2]

The decision of the Circuit Court of Appeals in our *Denver* case is in accord with the *New Haven* case on the jurisdiction and power of the Circuit Court of Appeals to reverse the District Court and order a plan remanded for adjustments whenever within the framework of a reorgan-

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[1] *In re New York, New Haven & Hartford R. Co.* (2nd C. C. A. 1945) 147 Fed. 2d 40, 48.

[2] *In re New York, New Haven & Hartford R. Co.* (1945) —— U. S. ——, 65 Sup. Ct. 1578, 89 L. Ed. 1553.

ization plan it is inequitable and unfair to one class of creditors. It is also in accord with the *New Haven* case upon the merits of using surplus cash to reduce senior debts, the redistribution of the securities thereby released among the other creditors and in having the adjustments made by the Commission.

The Milwaukee case (7th Cir.)

Similar adjustments and redistribution of securities released as a result of utilization of surplus cash to reduce senior claims have been made in the *Milwaukee* case in connection with the carrying out of the decision of this Court. It should be noted that in the *Milwaukee* case, the *New Haven* case, and in the *Missouri Pacific* and *Florida East Coast Ry.* cases, later reviewed, the Courts *considered and utilized the surplus cash and working capital accumulated after the Commission's plan came out.* Petitioners' argument that Courts *cannot* consider surplus working capital and cash accumulating after the date of the Commission's findings, or after the effective date of the Commission's plan, is contrary to all these decisions.

The manner in which the Commission made such adjustments in the Milwaukee plan is shown in the Commission's report[1] of December 6, 1943. At the end of the report, the Commission has made a "summary" of its changes, saying:

> "For the reasons stated, we conclude and find that the plan * * * should be adjusted, modified and corrected in the following respects, * * *
>
> * * * * * * *
>
> "(2) That approximately $52,038,036 be distributed in cash among the bondholders, as hereinbefore described, and as shown in appendices A and B * * *.
>
> "(3) That $7,096,336 of new first-mortgage bonds, be issued to creditors * * * as approximately repre-

[1] *Chicago, Milwaukee, St. Paul & Pacific Railroad Company Reorganization*, Second Supplemental Report, dated December 6, 1943, Finance Docket No. 10882, 254 I. C. C. 707; modified by Third Supplemental Report, dated April 10, 1944, 257 I. C. C. 223.

> senting the amount by which the claim of the Finance Corporation has been reduced, the payment of the loan of the Continental * * *.
>
> "(4) That by reason of the foregoing, adjustments and modifications be made in the allocation of certain new securities to certain classes of creditors * * * as shown in appendices A and B hereto." (254 I. C. C. 737).

The payment of the $52,000,000 cash in the *Milwaukee* case in reduction of senior claims and the redistribution of securities thereby released was approved by the Circuit Court of Appeals, 7th Circuit,[1] where the Court, in dismissing the appeal, said in part:

> "When the proceeding found its way back to the Commission, a large amount of cash had accumulated from the operation of debtors' railroad system, and the Commission ordered the distribution of some $52,000,000 of this cash to senior creditors * * * The action of the Commission in this respect was approved by the District Court." (145 Fed. 2d 302).

The District Court in our *Denver* case refused to follow the *Milwaukee* case in this respect. The Circuit Court of Appeals' decision in our *Denver* case, reversing the District Court, followed and conforms to the *Milwaukee* case.

The Florida East Coast case (5th Cir.)

The Circuit Court of Appeals' decision in our *Denver* case also conforms to the decisions in the *Florida East Coast* Case.[2]

In the *Florida East Coast* case, the Commission's plan (effective date December 31, 1940) fixed the new capitalization of the reorganized company at $37,000,000. The debtor had two mortgages. The old first mortgage secured

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[1] *In re Chicago, Milwaukee, St. Paul & Pacific Railroad Company* (7th C. C. A. 1944), 145 Fed. 2d. 299.

[2] *In re Florida East Coast Railway Co.* (D. C. S. Fla. 1943), 52 Fed. Supp. 420.

$12,000,000 of bonds which under the plan were to get 100% in new first mortgage bonds. The junior mortgage secured $45,000,000 of bonds; which under the Commission's plan were to get about 50% of their claim in new securities (10% of the claim in new second mortgage bonds, and about 40% in new common stock). The junior bonds were in a position similar to that of the junior General Mortgage Bonds in the *Denver* case (the treatment proposed for the Florida junior bondholders, however, was far less drastic).

By the time the Commission's plan in the *Florida East Coast* case came before the Court for consideration, the available net income had jumped from less than one million to over nine million dollars a year. The cash on hand had climbed from about 1¼ millions to over 17¾ millions.

The Court found that this great *accumulation* of cash not only made it necessary to give the old junior bonds more and better new securities, but required many other major changes. On motion, the Court sent the plan back to the Commission.

Judge Strum in the *Florida* case said in part:

> "This sum of $17,795,365 on hand October 1, 1943, is an existing fact, not a prophecy. * * *
>
> * * * * * * *
>
> "This cash represents net earnings of the company, on which the bondholders have a lien. To the extent that it is prudently available, the bondholders are entitled to the benefit of this surplus cash, either by having it applied in an equitable manner in satisfaction of their claims, or by having it otherwise definitely allocated by the Commission as a component part of the reorganization plan, so that it may be equitably applied to the best advantage of all concerned. * * * *To approve the present plan, ignoring the existence of this fund, would be improvident and inequitable to all security holders, especially to the minority. Such a course would not afford due recognition to the rights of the present bondholders, who have liens on these funds.*" (52 Fed. Supp. 422-3).

Pursuant to this decision, the Commission, on January 8, 1945,[1] modified the Florida East Coast plan, giving the Florida East Coast junior bondholders 100% of the principal of their claim in cash and new securities (in place of the 50%, largely in new common stock, provided in the earlier plan). The Commission accomplished this result, largely by using net earnings which had accumulated after the effective date of the Commission's Plan to pay off and reduce senior claims.

The Missouri Pacific case (8th Cir.)

The decision of the Court in the *Missouri Pacific* case[2] is along the same line. The District Court in 1941 had approved the Commission's plan. While appeals were pending from the approval order, the Commission submitted the plan to the creditors, and a majority of one or more classes of creditors rejected it. Thereafter the C. C. A. 8th Circuit, on appeal from the approval order, sent the case back for reconsideration. The plan then came before the District Court for confirmation on July 16, 1943.

The District Court held the plan inequitable and sent the plan back to the Commission for adjustments, suggesting that surplus cash on hand from wartime earnings be used further to reduce senior claims. The Court said in part:

> "* * * The revenues and earnings of this road, like others, has increased tremendously during the past few years, resulting in a sizable increment of cash. * * *
>
> * * * * * * *
>
> "It appears, therefore, * * * the accumulated cash might well be used to liquidate some or all of these especially preferred claims. * * *
>
> * * * * * * *

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[1] *Florida East Coast Railway Company Reorganization*, I. C. C. Finance Docket 13170, Second Supplemental Report, dated January 8, 1945. —— I. C. C. ——.

[2] *In re Missouri Pacific R. Co.* (D. C. E. D. Mo. 1943), 50 Fed. Supp. 936.

"* * * For * * * reasons, stated above, we must refer this matter back to the Interstate Commerce Commission. * * *" (50 Fed. Supp. 941, 942, 943).

Pursuant to Judge Moore's decision in the *Missouri Pacific* case, the Commission since then has certified an adjusted Missouri Pacific plan[1] carrying out the decision. The Commission took $30,000,000 to $35,000,000 of the cash from net earnings during trusteeship and reduced the senior claims, thereby improving the treatment of junior bondholders within the framework of the plan.

CONCLUSION

No "special or important reasons" exist in this case calling for the exercise of this Court's power of review or supervision. The determination by the Circuit Court of Appeals that the Plan is inequitable and unfair, and the reasons given therefor, are not in conflict, in any respect, with any decision of another Circuit Court of Appeals on the same matter or with the applicable decisions of this Court. That determination does not in any respect come within any other of the several classifications listed in this Court's Rule 38, paragraph 5(b).

Under facts showing that within the valuation and framework of the Commission's Plan, the proposed treatment of the junior General Mortgage Bondholders is unfair and inequitable and that their rejection of the Plan was reasonably justified, the Circuit Court of Appeals has jurisdiction and power to order the Plan referred back to the Commission for equitable adjustments.

The Circuit Court of Appeals' decision follows and conforms to all the decisions hereinabove reviewed and is merely a step towards accomplishing in the reorganization

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[1] *Missouri Pacific Railroad Company Reorganization*, Supplemental Report, dated July 4, 1944, Finance Docket 9918, 257 I. C. C. 479; modified by Third Supplemental Report, dated October 9, 1944, 257 I. C. C. 745.

of the Debtor what has already been accomplished by similar decisions in the reorganization of the Milwaukee, the New Haven, the Florida East Coast and the Missouri Pacific railroads.

The asserted questions alleged in the petition are based upon misconstruction of the Circuit Court of Appeals' decision and upon incorrect assumptions of fact as hereinbefore pointed out.

The Circuit Court of Appeals' decision upholds the valuation fixed by the Commission, makes no award of released securities or surplus cash to the General Mortgage bondholders or to any class of creditors, but leaves "all equitable adjustments" to the Commission, including the redistribution of released securities and surplus cash, so that claims of various classes of creditors will be taken care of "according to their priority in rank."

It is respectfully submitted in behalf of City Bank Farmers Trust Company, as Trustee under the Debtor's General Mortgage, that the petition for writs of certiorari filed by the Reconstruction Finance Corporation, Insurance Group Committee and others, should be denied.

Respectfully submitted,

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Of Counsel.

August 31, 1945.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

Nos. 278, 279, 280, 281 and 282

IN THE MATTER

of

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY,

Debtor.

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, *et al.*,

Petitioners,

against

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *et al.*,

Respondents.

(and the other four cases numbered above)

BRIEF IN OPPOSITION ON BEHALF OF THE DEBTOR-RESPONDENT, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY

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BRIEF IN OPPOSITION ON BEHALF OF THE DEBTOR-RESPONDENT, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY

In the Petition (No. 286) in the nature of a Cross-Petition for a writ of *certiorari* filed by the respondent, The Denver and Rio Grande Western Railroad Company (herein called the Debtor), for the purpose of bringing up the entire case in the event that this Court shall determine

to issue writs of *certiorari* pursuant to the Petitions (Nos. 278-282) of senior creditors it is stated:

> "To avoid duplication of the argument against the granting of that Petition this Petitioner adopts as its answer thereto such answer as shall be filed by the City Bank Farmers Trust Company, as Trustee under the Debtor's General Mortgage, reserving the right, however, to supplement such answer within the period permitted by the Rules of this Court."

City Bank Farmers Trust Company, as such Trustee has filed in lieu of an Answer an opposing Brief dated August 31, 1945. The Debtor concurs generally in that Brief. While the General Mortgage Trustee's Brief does not go as far as we think it should go in condemning as confiscatory the Plan of Reorganization to which this controversy relates and contains arguments from a strictly creditor standpoint which the Debtor's counsel might wish to qualify or to question in a clear-cut contest between creditor and equity interests, it is manifest that that is not this case. Here the issue is whether senior lien creditors are to be suffered to appropriate and to take for themselves not only the valuable equity represented by the Debtor's capital stock but also take 90% of the superior creditor investment secured by the Debtor's General Mortgage (Rec., pp. 36, 37; 183).

Only to a very limited extent—and even to that extent largely for the purpose of emphasis—does the Debtor feel that it might be helpful to this Court for it to supplement the comprehensive Brief filed by the General Mortgage Trustee.

The names of Reconstruction Finance Corporation and the Solicitor General of the United States appear in a conspicuous and perhaps misleading position at the head of the Petition. The Government as such is not interested in this proceeding. Let it be clearly understood therefore

that Reconstruction Finance Corporation is merely a secured creditor of the Debtor and is not otherwise interested in this proceeding and that no question involving its corporate powers or authority arises herein.

We agree with City Bank Farmers Trust Company that the Petition of the senior lien creditors is seriously inaccurate and attempts to state and present questions to this Court which do not arise under the decision of the Circuit Court of Appeals. Indeed we think this Court will find their Petition to be a mosaic of mistake, misunderstanding and misrepresentation. The statement appearing on page 2 that the decision of the Circuit Court of Appeals forces "substantial awards of cash and new senior securities to holders of old junior bonds" is typical. This statement is repeated not less than seven times at subsequent pages of their Petition.* The real facts are clear. The Interstate Commerce Commission's Plan gives nothing whatever to the junior Bonds but *common stock* and this is given for only 10% of their claim (Rec., p. 182). The District Court approved this treatment but the Circuit Court of Appeals held that this percentage of common stock could and must be increased as a matter of law to the extent possible within the limits of (a) the Commission's valuation of the Debtor's properties, and (b) the Commission's authorization of total reorganization capitalization. Common stock is the only currency required or permitted by the decision of the Circuit Court of Appeals. Should the Commission itself determine on reconsideration of the whole case in accordance with subsection (d) of Section 77 of the National Bankruptcy Act to revalue the properties so as to give effect to increased earning power due to heavy capital expenditures assuring greater efficiency and economy of operation; to the establishment of new productive industries of which the great $200,000,000 steel plant at Geneva is the outstanding example; to radical changes

* See pages 9, 10, 12, 13, 15, 16.

in traffic movements more nearly equalizing the loadings east bound and west bound; and to a dozen or more significant if not vital factors which should be given effect in order to avert a forfeiture of vested equity interests; then the increased valuation would be represented not by "cash and new senior securities" but only by a larger percentage of common stock. Even in that event part of the increased valuation may if the Commission so elects be represented by a junior issue of common stock designed only to pick up excess earnings in times of extraordinary prosperity (see Opinion of Judge HUXMAN, Rec., p. 253).

The Order or Decree of the Circuit Court of Appeals reverses two Orders of the District Court (Judge SYMES)—one an Order of the District Court approving the Plan of Reorganization certified to it by the Interstate Commerce Commission *before* it had been submitted for acceptance or rejection by creditors; the other an Order confirming the Plan *after* its submission to creditors and its rejection by a four to one vote of the holders of General Mortgage Bonds voting thereon (Rec., pp. 207; 224).

In order to override this veto and confirm the Plan it was necessary for the District Court judicially to determine *inter alia*:

> "* * * that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts" (11 U. S. C. A. Sec. 205(e)).

One of the relevant facts which standing quite alone would reasonably justify the action of the General Mortgage Bondholders in rejecting the Plan was the striking fact that over a period of steadily increasing prosperity the treatment accorded the General Mortgage Bonds had been revised downward from 100% treatment under the Plan first filed by the senior creditors and 33⅓% treatment offered under two prior Plans approved by the Interstate

Commerce Commission itself to 10% treatment under the Plan which these Bondholders wisely rejected. Their investment had waned under the erosion of steadily rising prosperity. This they knew was solecistic (see Plans dated June 15, 1937; July 11, 1939 and April 2, 1940).

A second relevant fact which also standing alone would reasonably justify the action of the General Mortgage Bondholders in rejecting the Plan was that the 10% treatment finally accorded them was to be represented by $4,354,816 par value of common stock taken at $100 per share which was actually less than one-half of the income earned *pendente lite* on the General Mortgage Bonds and lawfully impounded by the Mortgage Trustee (see Opinion of Judge PHILLIPS, Rec., p. 257). To this significant disclosure the senior creditor interests make the following *naive* answer:

> "Finally it should be noted that the claim of City Bank to a lien on any funds by impounding is without any basis. The Trustees from their appointment held all earnings for bondholders in the order of their priority and in addition petitions for sequestration were seasonably filed by the Indenture Trustees under all senior issues. Bonds secured by a senior lien on each half of the system, the Western Trusts and the Eastern Consolidateds have matured with a total claim of $76,551,000. All earnings are subject to a senior lien for the full payment of that whole amount before there can be anything for the General Mortgage bondholders and that has not been done. So this argument gives no special equity to the City Bank."

Of course the City Bank is not entitled to take in cash as against senior lienors the income earned by the Trustees applicable to General Mortgage interest. Such cash is primarily applicable to the matured principal of the senior lien debt. When so applied, however, the amount of the prior debt ahead of the General Mortgage Bonds

which must be taken care of out of the new capitalization authorized by the Commission is correspondingly reduced and this reduction at once makes available for them equivalent amounts of the new capitalization allocated to the senior lien Bonds. Since that had not been done the General Mortgage Bondholders had been maltreated and were in duty bound to reject the Plan.

A third relevant fact which reasonably justifies the action of the General Mortgage Bondholders in rejecting the Plan is the emasculation of their equity in the stock of the Utah Fuel Company. In spite of what is said in the Petition of the senior creditors (Rec., pp. 21-22) this stock (a) is given outright and irretrievably to the holders of the Bonds issued under the Rio Grande Western Consolidated Mortgage, and (b) is given to these Bondholders as a *bonus* without a disclosed valuation after they have been made whole.

Let there be no misunderstanding on this point.

In the Second Supplemental Report the Commission says:

> "In our opinion these bondholders are entitled to receive the beneficial interest in the Utah Fuel stock in addition to the reorganization securities allotted to them. The approved Plan so provides" (Rec., p. 136).

In the Third Supplemental Report the Commission reiterates:

> "Under the Plan the old bondholders would receive directly the ownership or the proceeds of the Fuel Company stock" (Rec., p. 167).

The stock of the Utah Fuel Company was originally pledged subject to withdrawal against the deposit of $6,000,000. This right of redemption was subsequently vested in The Western Pacific Railroad Corporation and the

Missouri Pacific Railroad Company in which Companies the naked legal title to the stock also was vested; but, by the same instrument or a contemporaneous instrument the stock and the entire equity of redemption were further pledged under the Debtor's Refunding and Improvement Mortgage and its General Mortgage in the order of their respective priorities (Rec., p. 52; Exs. 34-35).

Under the Commission's Plan the whole beneficial interest in the Utah Fuel stock is given *pro rata* to the holders of the Rio Grande Western Consolidated Bonds—in kind in case the Mortgage Trustee secures the release of the right to redeem at $6,000,000 as provided in an original agreement of pledge; in cash if the Mortgage Trustee is forced to foreclose in order to extinguish this right of redemption (Rec., p. 77).

To say, as to the senior creditors, that the Utah Fuel Company stock as Accommodation Collateral is left undisturbed by the Plan in accordance with the decision of this Court in *Ecker et al.* v. *The Western Pacific Railroad Company*, 318 U. S. 448, is to ignore all the facts of record to which we have referred. Apart from this, however, the basic rule asserted in that case is inapplicable here. That rule is that Accommodation Collateral can only be resorted to after exhaustion of the collateral directly pledged by the principal Debtor. Here there is an express agreement in favor of the Debtor's junior lien Bondholders and Preferred Stock that the stock of the Utah Fuel Company must be liquidated and applied to the payment of the Western Consolidated Bonds before there can be any resort to the other mortgage security. The General Mortgage Bondholders are entitled to require that this procedure be followed and are reasonably justified in rejecting a Plan which ignores their contract rights (Ex. 35—I. C. C. Rec., Vol. 7, p. 3171).

A fourth relevant fact which reasonably justifies rejection by the General Mortgage Bondholders of a Plan of

Reorganization that leaves 90% of their investment unprovided for is the Report of the Judiciary Committee of the House of Representatives showing that the threatened forfeiture is the consequence of a misunderstanding and misinterpretation of Section 77 on the part of both the Interstate Commerce Commission and the Courts. The entire investment may, however, be retrieved upon a reference of the proceeding back to the Interstate Commerce Commission after rejection under Subsection (c) for a new Plan under Subsection (d) if any *one* of three events shall occur: i, the passage of the proposed legislation; ii, a more liberal attitude on the part of the Interstate Commerce Commission, and iii, a modification by this Court of its opinions under Section 77 to conform to the interpretation of the Judiciary Committee. Each of these events was and is a just expectation and a reasonable probability. The legislation already has passed the House of Representatives with but a single dissenting vote and now awaits action of the Senate. The present policy of the Interstate Commerce Commission rests upon the vote of a bare majority—2 to 1—of Division 4 and can no longer be regarded as a fixed, stable policy. This Court has not hesitated to modify its previous opinions to correct mistakes or conform to changes in philosophy or even in ideology; and has always given great if not controlling weight to the formal report of a standing committee of Congress respecting legislation which it originated. Especially is this true of the Judiciary Committee of the House of Representatives.

In formulating Section 77 of the National Bankruptcy Act—which if properly interpreted by the senior creditors is the first legislation which has attempted to take from a pledgor the traditional protection of a public sale—Congress provided three safeguards against confiscation: *first*, a hearing and *quasi* judicial determination by the Interstate Commerce Commission; *second*, an independent judicial review which requires that the Court "be satisfied"

that the pledgor's property rights were fully protected; and *third*, an unconditional right of veto in one-third of each class unless such veto is exercised capriciously without reasonable justification (11 U. S. C. A., Section 205(d)(e)).

The first of these safeguards has proved valueless because the Interstate Commerce Commission acting through a bare majority of Division 4 has persistently subordinated rights of private property to the public interest in low cost transportation which may be assumed to be the ultimate outcome of artificially depressed carrier capitalization. The second safeguard—the independent judicial review of Commission action—has proved equally valueless for the reason as stated more fully in our Petition in No. 286 that this Court (we think erroneously) in the cases of *Ecker et al. v. The Western Pacific Railroad Corporation* and *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul and Pacific Railroad Company and others* has so limited the right of judicial review that the Court is required to be "satisfied" with almost any finding of value certified by the Interstate Commerce Commission even though the Court knows in fact that the Commission's valuation is confiscatory and is based upon the Commission's wholly undependable guess as to what may happen in the future. (See Opinion of Judge PHILLIPS, Rec., pp. 254; 260.)

The third and last safeguard—the right of veto in one-third of any class to which a Plan is submitted—is now under assault by Reconstruction Finance Corporation and the Group of Insurance Companies and Institutional Investors who are absorbing forfeited equities of junior creditors and stockholders to a point that threatens to become a widespread national scandal.* They say that no group of junior creditors may reject a Plan where the class is

* Reference is here made to Report of the Judiciary Committee of the House of Representatives, 78 Cong. 2d Session, Rep. No. 1615, Railroad Reorganizations under Section 77 of the Bankruptcy Act, Cong. Rec. June 27, 1945, Vol. 91, page 6915.

given the *residuum* of value remaining after senior creditors appear to have been made whole. They say:

> "It has been urged by dissenters, and was urged here by City Bank, that the 'not reasonably justified' phrase contemplates some more favorable provision than the basic canon of 'fair and equitable'. This would frustrate the purpose of the Act, for no Plan could lawfully award any class more than what is fair and equitable; yet each class could veto it unless it did."

That is to say, the right of veto means nothing.

This we categorically deny.

First of all it runs afoul of the rule that effect and meaning must be given to every clause of a statute. The finding of "fair and equitable" indispensable in *every* case would annul the right of veto in *any* case.

This was not the scheme of Section 77.

It must be remembered that Section 77 was designed as a new alternative to the equity procedure of foreclosure and sale. No Plan was to be consummated under this new procedure unless acceptable to two-thirds of each creditor class. The requisite percentage of any class might reject for any fair reason. They might properly reject because dissatisfied with the Commission's valuation, preferring to take their chances of securing a better result through foreclosure and sale. They might properly object because dissatisfied with the kind of capitalization prescribed by the Interstate Commerce Commission. They might properly object because the Plan brings in new properties which they think may prove burdensome.

Or, as is a vital factor in the instant case, they may object because, among other cogent reasons, the Plan reflects a stale record that is obsolete as the result of changed economic conditions and they think there should be a revised Plan on a record that is new and up to date.

If one or more of these reasons of which those mentioned are illustrative are of sufficient merit to impress one-third of a creditor class such class may reject the Plan.

The only qualification of this right is that they may not act capriciously or with an extortionate or improper objective. That is not this case.

As directed by the Circuit Court of Appeals this proceeding goes back to the Interstate Commerce Commission to proceed anew under subsection (d). This means that within six months the Debtor or any group of creditors must file a new Plan which unless *prima facie* impracticable must be set down for a hearing which the Interstate Commerce Commission may deplore but which Congress has ordained and *due process* requires.

The Petition for *certiorari* in Nos. 278-282 does not state a case within Rule 38 and should be denied.

September 5, 1945.

Respectfully submitted,

WILLIAM V. HODGES,
FRANK C. NICODEMUS, JR.,
Attorneys for Debtor-Respondent,
The Denver and Rio Grande
Western Railroad Company.

FILE COPY

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

Nos. 278, 279, 280, 281 and 282.

RECONSTRUCTION FINANCE CORPORATION; INSURANCE GROUP COMMITTEE, *et al.*,

Petitioners,

—against—

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *et al.*,

Respondents.

(and the other four cases numbered above)

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT.

BRIEF ON BEHALF OF RESPONDENT, CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE UNDER THE DEBTOR'S GENERAL MORTGAGE.

EDWARD E. WATTS, JR.,
PETER H. HOLME,
MILTON J. KEEGAN,
Counsel for Respondent,
City Bank Farmers Trust Company,
as trustee under the Debtor's
General Mortgage.

MITCHELL, CAPRON, MARSH,
ANGULO & COONEY,
DINES, DINES & HOLME,
Of Counsel.

February 15, 1946.

THE COURT PRESS, N. Y. C.

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Respondents.

(and the other four cases numbered above)

BRIEF ON BEHALF OF RESPONDENT, CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE UNDER THE DEBTOR'S GENERAL MORTGAGE.

Opinions Below.

The opinion of the Circuit Court of Appeals for the Tenth Circuit (R. 233-262)* is reported in 150 F. (2) 28; that of the District Court approving the Plan (R. 187-206) is not reported; that confirming the Plan (R. 213-224) is reported in 62 F. Supp. 384.

Introductory.

This is a railroad reorganization case under Section 77 of the Bankruptcy Act.

* R. 1-368, inclusive, is in Vol. I of record printed pursuant to 7-10-45 stipulation; R. 369-896, inclusive, is in Vol. II, and R. 897-1229 is in Vol. III of additional record printed pursuant to 11-26-45 stipulation. The annual reports and financial statements are in a fourth, un-numbered volume.

The Interstate Commerce Commission in June, 1943, proposed a plan (herein called the "Plan") for the reorganization of The Denver and Rio Grande Western Railroad Company (herein called the "Debtor"). The Commission, on April 26, 1944, after approval by the District Court and while appeals from the approval order were pending in the Circuit Court of Appeals, submitted the Plan to the creditors for acceptance or rejection, under Section 77(e) of the Act. The General Mortgage Bondholders voted to reject the Plan, with 79⅓% of the total vote voting for rejection. The result of the voting was certified to the District Court by the Commission on July 4, 1944 (R. 265-274).

On August 30, 1944, the District Court held a hearing on the question of whether the Plan should be confirmed notwithstanding its rejection, and on November 1, 1944, rendered its opinion confirming the Plan (R. 213-224), its final orders being entered on November 29, 1944. Various parties, including this respondent, the Trustee under the Debtor's General Mortgage, appealed from the confirmation order.

In the meantime, the Circuit Court of Appeals for the Tenth Circuit on November 13, 1944, had heard the appeals from the approval order, but it withheld its decision on those appeals until the whole case should come before it. The appeals from the confirmation order were argued before the Circuit Court of Appeals on March 14, 1945. On May 10, 1945, the Circuit Court of Appeals rendered its decision on the appeals from both orders.

On the General Mortgage Trustee's appeal from the confirmation order, the Circuit Court of Appeals held unanimously that the rejection vote of the General Mortgage Bondholders was "reasonably justified"

within the meaning of the statute, and should not be overridden.

On all the appeals, the Circuit Court of Appeals held unanimously that the Plan is not fair and equitable, that it does not afford due recognition to the rights of the General Mortgage Bondholders, that it discriminates unfairly in favor of the other classes of creditors and that it does not conform to the requirements of the law of the land regarding the participation of the various classes of creditors.

The Circuit Court of Appeals did not undertake to decide the related constitutional question, viz. whether Section 77(e) should be construed as giving the District Court power to confirm a reorganization plan after a *majority* of the voting creditors of any class have rejected it. Decision of that question was unnecessary because of (a) the holding that the rejection vote was not of an unreasonable nature which should be overridden, and (b) the holding that the Plan was not fair and not equitable, and did not conform to the requirements of Section 77(e) of the Act.

Question Presented.

The statute provides that if the Plan has not been accepted by at least two-thirds of those voting of each class of creditors entitled to vote on it, the District Court may (subject to "the right of judicial review" by the Circuit Court of Appeals) nevertheless confirm the Plan if the Court is satisfied and finds, after hearing:

1. that the Plan makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it;

2. that the Plan affords due recognition to the rights of each class of creditors and stockholders;

3. that the Plan does not discriminate unfairly in favor of any class of creditors or stockholders;

4. that the Plan will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; and

5. that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts.

The statute provides that any confirmation by the District Court shall be "subject to the right of judicial review" before it becomes binding on a class of creditors who have rejected the Plan.

The Plan now under consideration was not so accepted. On the contrary, it was rejected by 79.3% of the General Mortgage Bondholders who voted upon it.

The ultimate question presented is whether or not the General Mortgage Bondholders were "not reasonably justified", within the meaning of the statute, in rejecting the Plan.

That ultimate question requires examination of the terms of the Plan and its effect, to ascertain whether the General Mortgage Bondholders were accorded treatment to which a reasonable person, considering his own interests, could not reasonably object.

In answering that ultimate question, additional questions are presented relating to the compliance of the Plan with each of the statutory provisions above enumerated.

The unanimous Circuit Court of Appeals held (R. 253):

> "Under the admitted facts of the case, whether the plan complies with the requirement of Section 77(e) presents a pure question of law, and we are in nowise bound by the legal conclusions of the District Court in this respect. It is our conclusion that the plan fails to meet the requirements of Section 77(e). * * *."

It also held unanimously (R. 253):

> "* * * that the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, and that the District Court was without authority to confirm the plan in the face of their adverse vote."

The Statute.

Section 77(e) of the Bankruptcy Act (11 U. S. C. A., Sec. 205(e), pp. 93-5) provides in part:

> "* * * The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed * * * for acceptance or rejection, * * *. The Commission shall certify to the judge the results of such submission.
>
> "Upon receipt of such certification, * * * if the plan has not been so accepted by the creditors [*i. e.*, by * * * creditors of each class * * * holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported * * * as voting on said plan] * * *, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified

in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the Plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e) [i. e., * * * that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders; does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) * * *; (3) * * *.] * * * If the judge shall not confirm the plan, he shall * * * enter an order in which he shall either dismiss the proceedings, or * * * refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. * * *"

Section 77(f) of the Bankruptcy Act (11 U. S. C. A., Sec. 205(f), p. 95) provides in part:

"(f) Upon confirmation by the judge, the provisions of the plan and of the order of confirmation shall, subject to the right of judicial review, be binding upon * * * all creditors * * * who have not, as well as those who have, accepted it."

STATEMENT.

The Debtor's General Mortgage.

This respondent, City Bank Farmers Trust Company, is the trustee of the Debtor's General Mortgage, under which $29,808,000, principal amount, of General Mortgage Bonds are outstanding (R. 37). The total General Mortgage claim, including accrued unpaid interest of $43,740,155, as of the proposed effec-

date of the Plan, January 1, 1943, aggregated about 43½ million dollars (R. 183). The General Mortgage Bonds constitute almost one-fourth of the Debtor's entire indebtedness. They are the Debtor's junior bonds.

The holders of the General Mortgage Bonds voted, by 79.33% to 20.67% of those voting, to reject the Plan (R. 266).

There is no committee representing the holders of the General Mortgage Bonds. The holders are numerous; the individual holdings are small. This respondent, the General Mortgage Trustee, is the only representative of this class of creditors participating in the case. It made no recommendation to any bondholder as to how he should vote on the Plan (R. 337-8).

Notwithstanding these facts, holders of 21.6% (R. 268) of the outstanding General Mortgage Bonds cast their vote—enough to give a representative ballot as contemplated by Section 77, as amended by the August 27, 1935 amendments.

The Plan.

The Plan was proposed by the Interstate Commerce Commission in its Third Supplemental Report and Order dated June 14, 1943, 254 ICC 349 (R. 151-186). The Plan is in the alternative, with or without consolidation with the Denver & Salt Lake (an independent corporation sometimes called the "Moffat Road"). A summary of the Plan, without such consolidation, is given in Appendix B to the Commission's report (R. 183), a total capitalization of $143,528,027 being authorized (R. 159, 184). In this brief, to avoid confusion, figures applicable to reorganization without such consolidation always will be used.

The total capitalization of approximately 143½ million dollars may be obtained from the figures in the Commission's Appendix B (R. 183). It includes the notes to be held by the two collaterally-secured creditors, the Chase National Bank and the R. F. C., at their face amount only. The total does not include the authorized new securities to be issued by the reorganized Debtor and pledged as collateral* for those notes.

Under the Plan the General Mortgage Bondholders receive 10% of their claim in new common stock (being about 12% of the authorized common stock). The other 90% of their claim is wiped out. The Plan eliminates claims aggregating, as of the proposed effective date, over $118,300,000 (R. 36-7, 183), consisting of (a) about 39 million dollars of the General Mortgage claim, (b) the Debtor's unsecured indebtedness of about 440 thousand dollars, (c) the Debtor's preferred stock outstanding in the amount of 16½ million dollars, and (d) the Debtor's 300,000 shares of common stock, carried on the balance sheet at about 62½ million dollars.

As the Plan has been construed, were it now to be put into operation, the capitalization of the reorganized Debtor would be substantially less than the 143½ million dollar amount authorized by the Commission.

This reduction results from the elimination of some of the senior debt by application of "surplus cash" earned and accumulated since the Plan was proposed by the Commission.

For purposes of comparison it might be noted that the Debtor's Trustees carry the Debtor's assets on

*A large part of the collateral for the R. F. C. note consists of securities not issued by the Debtor (R. 18).

their balance sheets at $302,692,146.59,* of which over 239 million dollars represents road and equipment and over 19 million dollars is in cash or temporary cash investments.

The earlier plans.

At least ten other reorganization plans have been proposed for this Debtor since the institution of these proceedings. Certain features of the several plans may be summarized as follows:

Plan†	Date proposed	Authorized capitalization (A)	Percentage of claim of General Mortgage Bonds provided for in new stock (B)	Percentage of total authorized common stock allocated to General Mortgage Bonds
Debtor's	7 29 36	$158,747,766	100%	0
Insurance Group I	6 15 37	149,732,966D	100%	100%
Examiner's I	8 12 38	137,154,585	50%	50%
ICC I	7 31 39	135,788,354	33⅓%	33%
ICC II	4 11 40	135,788,354	33⅓%	33%
Discussion	1 6 41	135,005,436E	50%	44%
District Court's	3 6 41	136,960,724	32.99%	35.2%
Examiner's II	9 2 41	157,540,952	33⅓%	32.6%
Insurance Group II	10 8 41	161,631,934	47.42%	46%
ICC III	7 27 42	142,846,612	5%	5%
ICC IV (the "Plan")	6 28 43	143,528,027F	19%	12%

* Income Account and Financial Exhibit for the period ended December 31, 1944, p. 5.

† For key to plans see continuation of this footnote, p. 10.

A. Figures based upon reorganization of the Debtor *without* consolidation with the Denver and Salt Lake.

B. The Debtor's plan allotted preferred stock to the General Mortgage Bondholders; all subsequent plans common stock. The percentages given relate to the entire claim, including interest to proposed effective date.

C. The Debtor's plan gave General Mortgage Bonds 80.1% of the new preferred stock to be outstanding.

D. Exclusive of warrants for old stock.

[Footnotes continued on following page.]

As indicated in the foregoing table, these plans have provided varying treatment for the General Mortgage

(Footnotes continued from preceding page.)

E. Plus $10,000,000 of claims to be paid in cash.

F. Because of reductions in senior claims outstanding since 6, 28 43, the amount to be outstanding would now be less than 140 million dollars.

Key to Plans

"Debtor's"—Debtor's original plan of July 28, 1936—filed July 29, 1936, proposed effective date January 1, 1937 (R. 401-426, 426A).

"Insurance Group I"—First plan of Insurance Group Committee—filed June 15, 1937, proposed effective date January 1, 1937 (R. 427-466, 458A).

"Examiner's I"—I. C. C. Examiner Jameson's first plan—filed August 12, 1938, proposed effective date June 30, 1938 (R. 466-526, 518).

"ICC I"—Commission's first plan of July 11, 1939, filed July 31, 1939, proposed effective date June 30, 1938 (R. 29-97, 352).

"ICC II"—Commission's modified plan of April 2, 1940—filed April 11, 1940, proposed effective date June 30, 1938 (R. 98-112).

"Discussion"—So-called discussion plan of October 28, 1940—proposed as a compromise by Insurance Group Committee after conferences with R. F. C.—filed January 6, 1941, proposed effective date June 30, 1938 (R. 549-559, 554A).

"District Court's"—District Court's plan (R. 559-568, 568A) in Opinion of and filed March 6, 1941, proposed effective date June 30, 1938. (The District Court also tentatively suggested a plan outline in its preliminary opinion of December 6, 1940 (R. 526), calling a conference of the parties. After the conference that outline was superseded by the Court's plan in its March 6, 1941 final opinion on the Commission's 1940 plan.)

"Examiner's II"—I. C. C. Examiner Jameson's plan of August 26, 1941—filed September 2, 1941, proposed effective date January 1, 1942 (R. 569-604, 604A).

"Insurance Group II"—Insurance Group plan filed October 8, 1941, proposed effective date January 1, 1942 (R. 604B).

"ICC III"—Commission's plan of July 13, 1942—filed July 27, 1942, proposed effective date January 1, 1942 (R. 113-150, 353-6).

"ICC IV" (in this brief usually called the "Plan" but designated as "ICC IV" in the charts)—Commission's plan of June 14, 1943—filed June 28, 1943, proposed effective date January 1, 1943 (R. 151-186).

Bonds. The first two plans gave them 100% of their claim in new preferred or Class A common stock. The present Plan gives them 10% of their claim in common stock. The three plans proposed at various times by the senior creditors offered the General Mortgage Bondholders a maximum of 100% and a minimum of 47.42% of their claim in new stock.

The treatment proposed in these eleven plans and the current earnings of the property in the years in which the several plans were proposed are tabulated as follows:

Date of plan proposal	Plan	Amount of common stock provided on total General Mortgage claim	Current income available for interest in year plan proposed **
7 29 36	Debtor's	100% *	$ 1,626,179
6 15 37	Insurance Group I	100%	— 294,880
8 12 38	Examiner's I	50%	10,018
7 31 39	ICC I	33⅓%	1,717,298
4 11 40	ICC II	33⅓%	2,626,847
1 6 41	Discussion	50%	4,358,182
3 6 41	District Court's	32.99%	4,358,182
9 2 41	Examiner's II	33⅓%	4,358,182
10 8 41	Insurance Group II	47.42%	4,358,182
7 27 42	ICC III	5%	17,180,067
6 28 43	ICC IV	10%	11,766,741
1 1 44	Submission of Plan to Gen. Mtge. Bonds		$10,025,132

* Preferred stock.

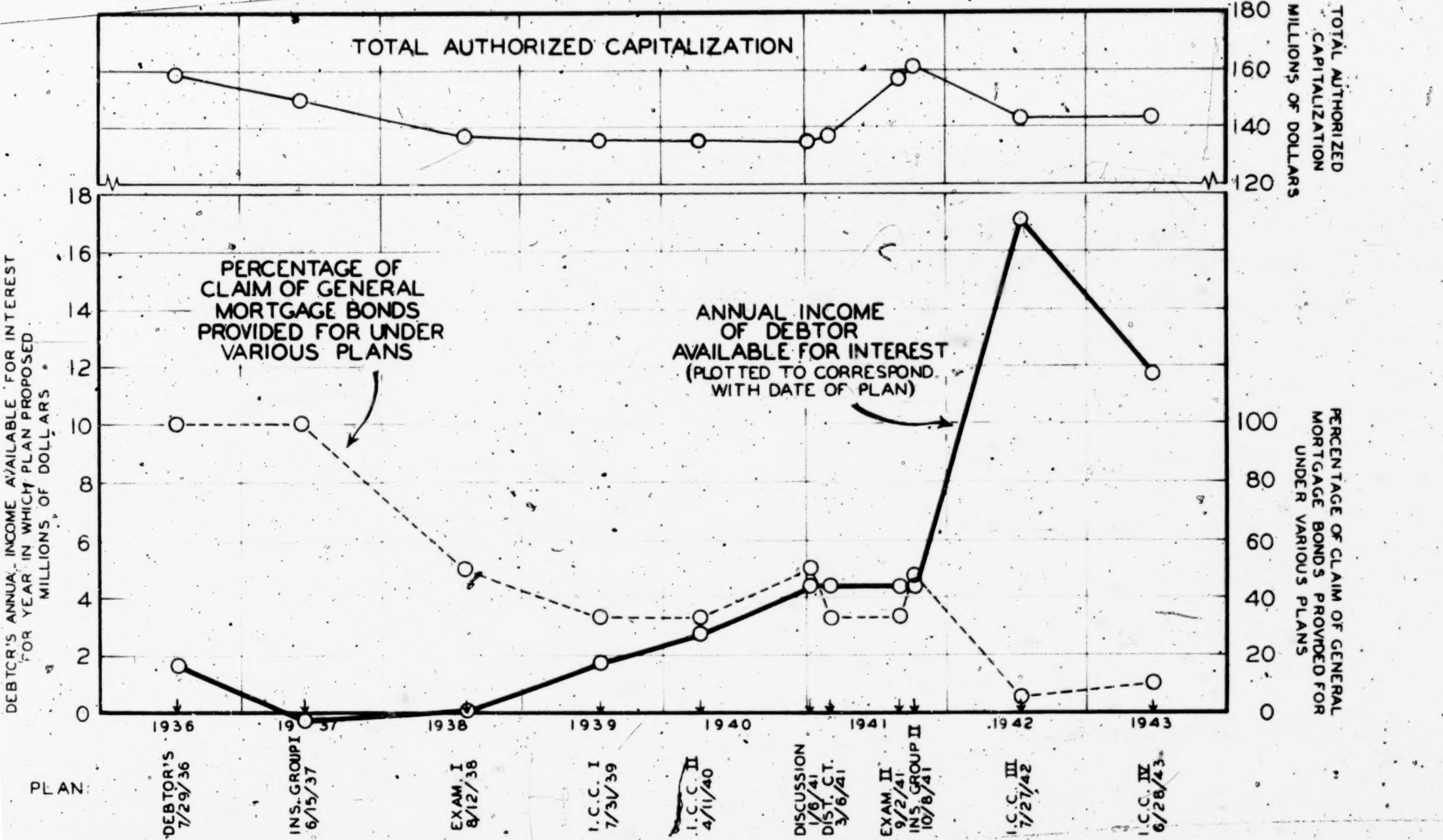
** See more detailed earnings table below (this brief 18).

The treatment proposed and the current earnings in each of such years are also shown graphically, and compared, on the chart opposite this page. The broken line connects the eleven points which show the percentage of the total General Mortgage claim provided for in each of the eleven plans (scale at right). The heavy line connects the eleven points which show the available income earned in the respective years in which the eleven plans were proposed (scale at left). This chart shows that, as the earnings have improved, the treatment proposed for the General Mortgage Bonds has steadily worsened. The unbroken line at the top shows the authorized capitalization in the eleven plans, which has not fluctuated greatly, notwithstanding the extraordinarily heavy improvement program which has been carried out, and paid for out of the earnings which accrued during the pendency of these reorganization proceedings—earnings which might have been used, but were not used, to pay interest on the indebtedness which is prior in lien to the General Mortgage.

The improvement program.

During the reorganization period the Debtor's Trustees have carried on an improvement program of extraordinary proportions. When the magnitude of the program first became apparent, the General Mortgage Trustee, on July 17, 1936, filed its answer to a petition of the Debtor's Trustees for authority to borrow money for the purpose of carrying out the initial portion of the program (R. 398-401). This respondent urged the Court to eliminate from the schedules of proposed improvements all items not shown to be essential for the safe operation of the property or its preservation (R. 400). After hearing,

TREATMENT OF GENERAL MORTGAGE CLAIM PROPOSED IN ELEVEN REORGANIZATION PLANS COMPARED WITH DEBTOR'S INCOME AVAILABLE FOR INTEREST IN YEAR OF PROPOSAL



THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, DEBTOR

the Court overruled the objections of this respondent and directed its Trustees to proceed with the program.

The decision of the District Court and its Trustees to proceed with this program and to divert earned income, otherwise available for payment of interest on the senior bonds, into permanent additions and betterments of the Debtor's property, much of it at a low cost, turned out well for the trust estate.

The extent of the program can be determined by a study of the annual reports which show the "increase" in investment in road and equipment, for the years in question, in special tables. It appears from the following tabulation that up to July 31, 1944 (the end of the last month prior to the confirmation hearing), the additions and betterments charged to capital account aggregate over 43 million dollars and about 11 million dollars more, charged to income, was spent during the same period in connection with these improvements, making a total of over 54 million dollars so expended:

Period	Expenditures incident to improvement work	Additions and betterments charged to capital accounts	Total
1935 (last 2 mos.)	$ 30,000*	$ 90,000*	$ 120,000*
1936	2,910,726†	2,079,254	4,989,980
1937	1,450,349	4,270,728	5,721,077
1938	559,926	2,877,090	3,537,016
1939	1,129,075	2,970,334	4,099,409
1940	1,056,410	3,363,452	4,419,862
1941	1,180,750	6,071,534	7,252,284
1942	950,057	6,127,558	7,077,615
1943	1,014,432	9,772,823	10,787,255
1944 (first 7 mos.)	700,000*	5,688,740	6,388,740
1944 (to 12/31/44)	1,464,059	6,827,071	8,291,130
Totals (to 8/1/44)	$11,081,725	$43,291,513	$54,373,238
Totals (to 12/31/44)	$11,845,784	$44,449,844	$56,295,628

* Estimated.

† Includes $2,000,000 for maintenance work in 1936 deferred in prior years.

The figures in the foregoing table relate to improvements on the Debtor's property only and do not include the additions and betterments on leased lines (the Debtor's subsidiaries), or expenses incident thereto. If these were included, it would increase the total by about 2½ million dollars.

The petitioners object to the 43 million dollar figure cited by the Circuit Court of Appeals (R. 243), stating that it does not give a full picture because it does not reflect retirements during the same period. The retirements during that period, *i. e.*, up to August 1, 1944, aggregate about 13 million dollars. That amount could be subtracted and there would still remain a net gain for capital account of more than 30 million dollars. It is submitted, however, that such a subtraction would not be fair or accurate. A large part of the retirements in question were abandonments. It was pointed out in the expert testimony of the witness, Miles C. Kennedy (R. 332), that the Commission does not authorize abandonments until it is satisfied that the property to be abandoned has been a drain on the system and has been consistently losing money. If a useless and money-losing piece of road is abandoned, that particular transaction constitutes gain and not loss with respect to the Debtor's net value for reorganization purposes, notwithstanding the fact that the book value of the abandonment decreases the total book value of the property.

The senior creditors.

The petitioners, who would have the Plan confirmed notwithstanding its rejection by the General Mortgage Bondholders, are senior creditors. Under the Plan they are to receive the full face amount of their respec-

tive claims, principal and accrued interest, in Plan securities (R. 183). The senior creditors are to receive outright (except for 12% of the common stock) the Debtor's railroad system. It is a greatly improved railroad. It is a railroad system on which, up to July 31, 1944 about 54 million dollars of earnings accumulated during the pendency of the proceedings had been spent on additions and betterments over and above normal maintenance.

Because the available earnings have been plowed back into property, in betterments and improvements, instead of being used to pay interest on the claim of the senior creditors during the period between November 1, 1935 and December 31, 1944, the claim of the senior creditors has increased by about 40 million dollars, on account of accrued interest, and new securities of that total face amount, which would otherwise have been available for distribution to the General Mortgage Bondholders, have been re-allocated to the senior creditors. This resulted from the fact that there has been no substantial increase during the pendency of the proceedings of the total amount of securities to be authorized for the reorganized Debtor, even though, by the investment of approximately 54 million dollars, the railroad to be owned by the holders of the new securities, and the earning power of that railroad, have been vastly improved. Thus the treatment of the senior creditors in the Plan is both quantitatively and qualitatively better than that provided in the earlier plans.

Under the Plan, one class of senior creditors is to receive, in addition to 100% of its total claim in new securities, all of the stock of Utah Fuel Company, on which stock this respondent has a junior lien.

The institutions which are members of the Insur-

ance Group Committee, one of the principal petitioners, own no General Mortgage Bonds (R. 428). The same is true of the R. F. C. (R. 39). The other petitioners are trustees of the senior mortgages.

The impounding petition.

The General Mortgage Trustee acted promptly to make sure that any net income from the mortgaged property should be impounded for the benefit of the General Mortgage Bondholders. Its impounding petition was filed on November 19, 1935, a few weeks after the institution of the reorganization proceedings (R. 376-398, 397).

After that impounding petition was filed and up to the end of 1944 the property which is subject to the General Mortgage lien produced earnings of approximately 50 million dollars, or over 9 million dollars more than enough to cover full interest requirements on the senior securities—the surplus to that date being about $9,389,418.

Earnings.

The Debtor's earnings record has been good except for the depression years. In the six years preceding the depression, 1925 to 1930, inclusive, the Debtor's net income available for interest ranged between $6\frac{1}{2}$ and $8\frac{3}{4}$ million dollars annually (R. 348). The interest requirements for all creditors senior to the General Mortgage total between 4 and $4\frac{1}{2}$ million dollars annually (R. 349). The annual interest charges on the General Mortgage Bonds amount to about $1\frac{1}{2}$ million dollars.

Since the end of 1941 (by which time a substantial

part of the 43-million-dollar expenditure for additions and permanent improvements had been made), the Debtor's net available for interest has been running between 10 and 17 million dollars annually (R. 280-1, 348, 349). There is undisputed testimony that the improvements can be expected to yield a return of 10% to 15% or even more (R. 346-7). That would indicate an increase in earnings, resulting from the improvements, of between 4 and 6½ million dollars in an average year.

As already pointed out, from the institution of these reorganization proceedings in 1935 up to the end of 1944 the Debtor's income available for interest has exceeded total interest requirements for all creditors' claims senior to the General Mortgage Bonds by more than 9 million dollars. Thus there has been an average of over one million dollars a year of earnings available for the General Mortgage Bonds, being approximately two-thirds of the contract interest requirements of that junior issue. This period involves the six worst years in the present company's history (R. 348).

The figures were tabulated in this Respondent's Exhibit 10 (R. 349) introduced at the confirmation hearing. With a slight correction in the figures for 1944 (which had been estimated), this table showed the following:

Year	Income available for interest*	Interest requirements for securities senior to General Mortgage*	Income (or deficit) after interest on senior securities
1935 (last 2 mos.)	$ 405,418	$ 701,818	$ — 296,400
1936	1,626,179	4,182,219	— 2,556,040
1937	— 294,880	4,160,664	— 4,455,544
1938	10,018	4,179,725	— 4,169,707
1939	1,717,298	4,184,227	— 2,466,929
1940	2,626,447	4,206,933	— 1,580,086
1941	4,358,482	5,169,696	— 811,574
1942	17,180,067	4,382,701	+12,797,366
1943	11,766,791	4,368,551	+ 7,398,160
1944 (first 7 mos.)	5,992,635	2541,745	+ 3,450,890
1944 (12 mos.)	10,025,132**	4,495,020	+ 5,530,112
Total for whole period 11 1 35 to 12 31 44	$49,420,972	$40,031,554	$+ 9,389,418

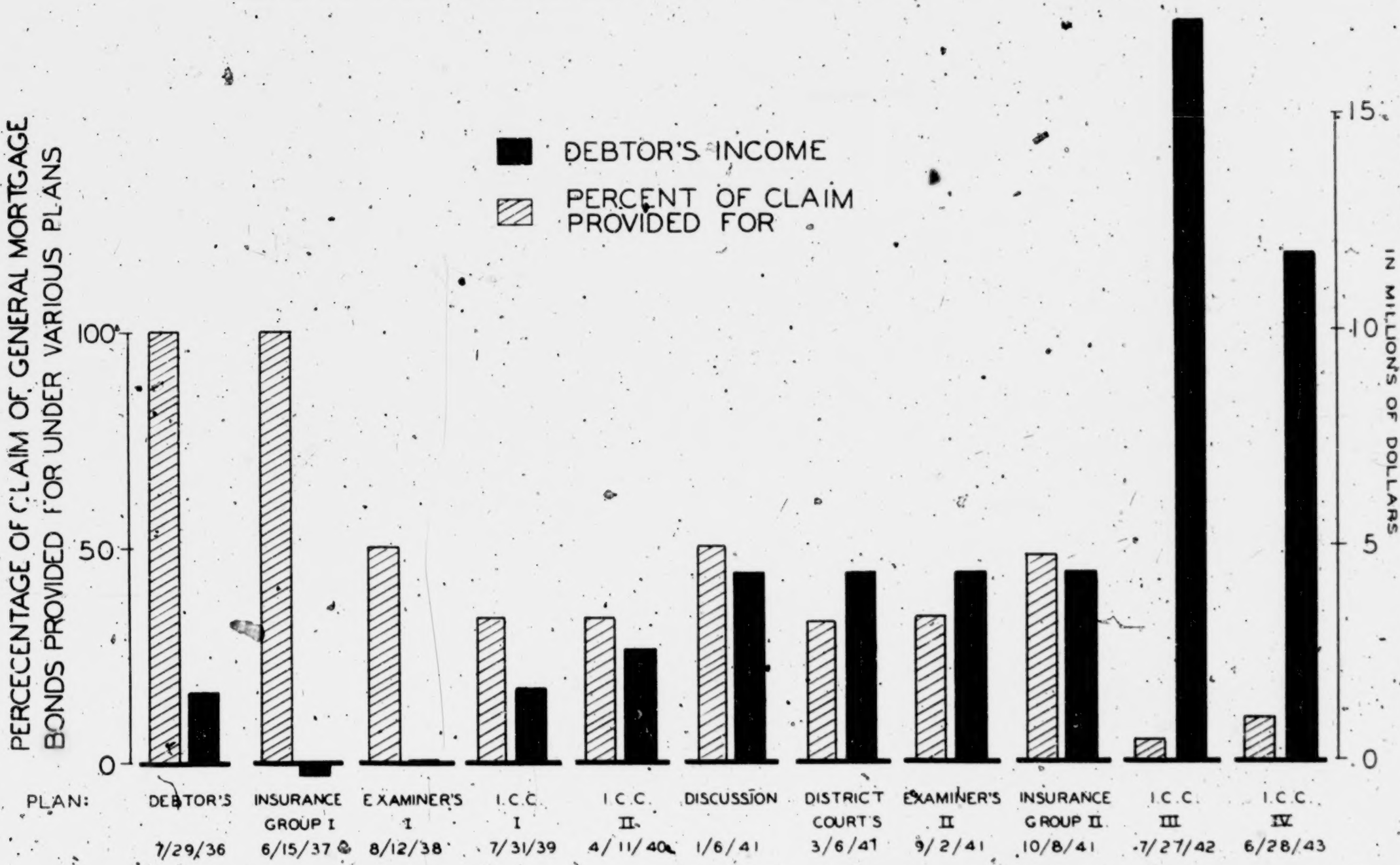
The $49,420,972 of income available for interest shown in the foregoing tabulation is an existing fact; it is not dependent on hypothetical future earnings. It has been retained in the Debtor's estate and is today in existence—either in the form of cash and government bonds or in the form of permanent capital improvements.

What has happened during the course of the reorganization period is shown graphically on the chart opposite the next page, which compares the treatment of the General Mortgage Bonds proposed in the eleven

* Interest figures include interest on unfunded debt. The source of the figures up to August 1, 1944 are Trustees' Annual Report, 1943, page 32, computed as directed by T. A. Thompson, General Auditor (R. 279-89) and August 1943 and July 1944 Income Account Statements.

** The figure in the Trustees' December 1944 Income Account Statement, p. 1, is $8,490,992.45. It has been adjusted for this table and brief by adding back the item of "Delayed Income Debits" which appears for the first time in the December 1944 Statement, and amounts to $1,534,139.75. This item is accumulated rental on the Cut-off during *earlier years* of trusteeship, *all* paid in 1944 to the Trustee of the wholly-owned Subsidiary Debtor. This item in essence represents funds transferred from one pocket to the other and should not be deducted from Gross Income in arriving at a true representation of the Debtor's income available for interest

TREATMENT OF GENERAL MORTGAGE CLAIM PROPOSED IN ELEVEN REORGANIZATION PLANS COMPARED WITH DEBTOR'S INCOME AVAILABLE FOR INTEREST IN YEAR OF PROPOSAL



THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, DEBTOR

plans previously described with the current earnings of the property in the years in which the several plans were proposed. Each set of two bars relates to one of the eleven plans. The lightly-shaded bar of each set shows the treatment proposed in the plan in question (scale at left). Thus, the first two plans proposed giving the General Mortgage Bonds new stock equal to 100% of their claim, principal and accrued interest; the most recent Plan proposes giving the General Mortgage Bonds 10% of their claim. The solid-black bars show the Debtor's income available for interest as of the year in which the particular plan in question was proposed (scale at right). Thus, in 1937, when the Insurance Group proposed its first plan (providing that the General Mortgage Bondholders should receive 100% of their claim in new Class A common stock), there was a net deficit before interest. In 1943, when the Plan now under consideration was proposed, the income available for interest amounted to $11,766,711.

The 1944 income available for interest is not shown on this chart although the figures were available in the courts below. As shown on the previous table, the 1944 available income was $10,025,132. It was in 1944 that the General Mortgage Bondholders were called upon to vote on the question of accepting or rejecting the Plan, which asked them to accept 10% of their total claim in new common stock in full satisfaction of their claim.

In an effort to show insufficiency of earnings the petitioners present their Appendix F, dealing with many years prior to these proceedings. Assuming their arithmetic correct, that table bears no relation to the actual facts regarding interest coverage.

On the next page is an interest-coverage table in which we have limited ourselves to the figures actually recorded in the annual reports. The earliest year for which figures are available in the record is 1915. For the years 1915 through 1944 we have taken from the annual reports (I) total operating revenues, (II) net operating revenues, (III) earnings available for interest on funded debt (after all taxes and interest on unfunded debt), (IV) interest on the senior bonds, and (V) the amount available for interest on the General Mortgage Bonds.

The General Mortgage Bonds were not issued until 1924. Full interest requirements on the General Mortgage Bonds, being $1,490,400 per year (5% on $29,808,000) would amount to $44,712,000 for the period 1915 to 1944, inclusive. Column V shows that the actual amount earned by the Debtor, available to cover such interest, was $54,409,082, or $9,697,082 more than required.

If we are to delve into the record of earnings for a period long prior to these proceedings, the only figures entitled to serious consideration are the actual results of operation. It is meaningless, if not misleading, to present a table, such as the petitioners' Appendix F, to which various hypothetical factors and assumptions have been applied for the purpose of building up a theoretical deficit of 60 million dollars, which might have resulted under a chosen set of circumstances but which actually bears no relationship to reality. The fact is that the earnings of the Debtor, after all senior interest, have exceeded the amount of all interest on the General Mortgage Bonds for this 30-year period by $9,697,082.

Earnings available for interest on all bonds senior to the General Mortgage and for interest on the General Mortgage Bonds for the period 1915 to 1944.

	I	II	III	IV	V
	Total Operating Revenues	Net Operating Revenues	Available for Interest on Funded Debt	Interest on All Bonds Senior to General Mortgage	Available for Interest on General Mortgage Bonds
1915	23,138,797	8,892,439	8,354,335	3,313,465	5,040,870
1916	25,464,486	10,588,131	10,019,696	3,305,965	6,713,731
1917	28,423,138	8,694,709	7,722,220	3,282,865	4,439,355
1918	31,352,214	6,058,789	6,995,867	3,279,740	3,716,127
1919	33,016,257	7,359,285	5,732,699	3,279,740	2,452,959
1920	40,590,345	8,037,098	9,508,213	3,279,740	6,228,473
1921	32,621,419	4,875,329	3,303,907	3,279,740	24,167
1922	33,350,564	7,945,789	5,166,973	3,279,740	1,887,233
1923	34,587,497	4,556,828	2,819,749	3,418,958	*—599,209*
1924	33,011,558	4,420,401	2,394,626	3,816,410	*—1,421,784*
1925	33,629,464	8,835,215	6,788,296	3,619,229	3,161,067
1926	34,039,309	9,415,995	7,705,670	3,665,553	4,040,117
1927	36,124,169	8,041,953	6,472,257	3,690,371	2,775,886
1928	33,200,656	8,758,241	7,314,899	3,870,517	3,444,382
1929	34,828,669	10,293,502	8,811,533	3,890,698	4,920,835
1930	29,747,537	9,051,736	7,068,617	3,893,936	3,174,681
1931	23,484,818	7,061,678	5,142,666	3,877,918	1,264,748
1932	17,560,621	4,850,144	2,739,793	3,833,089	*—1,093,810*
1933	17,412,794	5,225,370	3,140,746	3,789,299	*—648,553*
1934	19,246,850	4,601,589	2,260,019	3,745,491	*—1,485,472*
1935	20,944,250	4,808,762	1,929,183	3,707,582	*—1,778,399*
1936	25,599,309	4,660,350	1,422,333	3,678,373	*—2,256,040*
1937	26,781,992	2,656,275	*—798,596*	3,656,948	*—4,455,544*
1938	23,404,171	3,661,691	*—195,698*	3,676,009	*—4,469,707*
1939	25,073,039	4,809,678	1,213,382	3,680,511	*—2,466,929*
1940	26,219,195	5,740,324	2,120,496	3,700,582	*—1,580,086*
1941	31,572,624	7,353,504	2,910,045	3,721,559	*—811,514*
1942	54,475,496	23,214,802	16,529,932	3,732,566	12,797,366
1943	70,194,002	24,392,502	11,116,576	3,718,416	7,398,160
1944	70,346,987	20,569,809	7,699,535	3,703,563	3,995,972
1915-1944	966,130,236	248,333,838	162,804,175	108,395,093	54,409,082

From 2nd Column, Top Table, p. 29, 1935, 1943 and 1944 Annual Reports
From 6th Column, Top Table, p. 29, 1935, 1943 and 1944 Annual Reports
From 9th Column, Top Table, p. 32, 1935, 1943 and 1944 Annual Reports (this is after interest on unfunded debt)
From Total Interest on Funded Debt (1st Column, Middle Table, p. 32, 1935, 1943 and 1944 Annual Reports) less interest on General Mortgage Bonds (6th Column, Middle Table, p. 32, 1935, 1943 and 1944 Annual Reports) or interest on Adjustment Mortgage and First and Refunding Mortgage Bonds (1st and 2nd Columns, Bottom Table, p. 32, 1935 Annual Reports) in exchange for which General Mortgage Bonds were issued in the 1924 Reorganization.

One important factor to which neither the petitioners' Appendix F nor the foregoing table gives any weight is the extraordinary improvement program carried out during the last few years. It should add 4 to 6 million dollars, or more, to the Debtor's income on the basis of the expert testimony of Miles C. Kennedy (R. 316-7).

In another effort to show insufficiency of earnings, the petitioners say that "For many years one of the most pervasive and fundamental trends in the railroad industry has been the seemingly inexorable advance in unit costs". This assumption appears repeatedly (petitioners' brief 16, 17, 33, 60, 61, 62, 79). What are the facts? In the yearbook of Railroad Information—1944 edition, published by the Eastern Railroad Presidents' Conference Committee on Public Relations, operating revenues and operating expenses of the Class I railways are tabulated from ICC figures for typical years from 1916 to 1943. From this table, it will be noted that there has been an over-all decrease in the ratio of operating expenses to operating revenues, as follows:

1918	81.6%	1935	75.1%
1921	82.7%	1936	72.3%
1926	73.2%	1937	74.9%
1928	72.5%	1938	76.3%
1929	71.8%	1939	73.0%
1930	74.4%	1940	71.9%
1931	77.0%	1941	68.5%
1932	76.9%	1942	61.6%
1933	72.7%	1943	62.5%
1934	74.6%		

Thus, the fact is that improvements in the art of railroading are steadily decreasing the operating ratio in

spite of the alleged "*seemingly* inexorable advance in unit costs" (emphasis supplied).

Cash and working capital.

The cash, current assets and net working capital of the Debtor's Trustees have shown a favorable trend throughout the period of these proceedings, and the improvement since January 1, 1943 (the proposed effective date of the Plan) has been impressive. For convenience, the following table has been prepared giving the figures which appear in the annual reports:

As of 12/31	Cash	Current assets	Current liabilities	Net working capital
1935	$ 1,257,943	$ 5,966,667	$15,545,219*	*$−9,578,552*
1936	1,282,525	8,025,321	11,446,128*	*−3,420,807*
1937	1,386,679	9,640,322	11,972,533*	*−2,332,211*
1938	2,337,018	8,229,639	7,867,770*	361,869
1939	3,284,015	8,622,087	8,166,536*	455,551
1940	4,328,184	9,553,783	8,412,669	1,141,114
1941	4,460,157	11,828,589	10,292,313	1,536,276
1942	10,850,150**	20,983,653	14,172,576	6,811,077
1943	20,721,925**†	33,915,864†	23,517,780	10,398,084†
1944	19,142,676**‡	32,665,501‡	20,539,638	12,125,863‡

The figures in the last column, showing net working capital, are obtained by subtracting current liabilities from current assets.

From the above it appears that as of January 1, 1943 (the proposed effective date of the Plan) the

* The first five figures under "current liabilities" were obtained by subtracting from the annual report figures for those years the items of "Interest Matured Unpaid" and "Funded Debt Matured Unpaid"; in the later annual reports those two items are not listed as current liabilities.

** Includes temporary cash investments.

† Does not include $3,751,995 set aside for deferred maintenance (R. 278; 1943 annual report, p. 12).

‡ Does not include $5,652,150 set aside for deferred maintenance (Income account and financial exhibit, December 31, 1944, p. 5).

net working capital was $6,811,077 and included in the current assets was cash amounting to $10,850,150. By the end of 1944 both of these figures had almost doubled.

Considering the whole period of the reorganization proceedings, the net working capital position has improved by $21,704,415 and the cash position in the meantime has improved by $17,884,733—if we exclude the sum of $5,652,450 set aside in account No. 704½ as "Maintenance Funds"—and by $23,536,923 if that special account is included.

The Circuit Court of Appeals (R. 247) points out:

> "We think it is apparent from the record that there were current assets on hand consisting of cash and securities in excess of what was needed for the efficient operation of the road. * * * we cannot disregard the fact that these huge surpluses actually exist. Their existence is an accomplished fact. * * * We think any plan which fails to take this into account and which gives the Senior Bondholders their claims in full by substantially delivering the road to them, and gives them the surplus cash actually on hand * * * is inherently inequitable and unfair, so long as there are classes of creditors whose claims are not fully satisfied."

The Circuit Court of Appeals further points out (R. 248):

> "* * * In his order of September 13, 1943 [nine months after the effective date of the Plan], directing the payment of the Junction Bonds in cash, the [District] court said: 'The trustees having on hand an amount of cash *far in excess** of

* Italicized in original; unless otherwise indicated, all emphasis in quotations is supplied.

the needs of reorganization expenses, including working capital * * *."

The Junction Bonds.

Of the 142½-million-dollar capitalization authorized in the 1943 Plan, about 2¾ million dollars of new senior securities were to be issued in exchange for the Junction Bonds (the First Mortgage Five Per Cent Bonds of The Rio Grande Junction Railroad Company, a wholly-owned subsidiary of the Debtor, owning that part of Debtor's main line from Rifle to Grand Junction, Colorado). Of these, $2,123,916 are new fixed-interest bonds and $634,417 are new income bonds (R. 183).

Some nine months after the proposed effective date of the Plan, the District Court directed that the Junction Bonds be paid or purchased by the application of "surplus cash" (R. 262, 263, 264-5). In that way, the first lien upon the Junction property, amounting to approximately 2¾ million dollars, has been eliminated—without issuing any of the 2¾ million dollars of authorized Plan securities which the Commission had allocated to that particular purpose and without depleting the cash below the amount contemplated in the Plan. After the application of this surplus cash, more cash and "net current working capital" remained than were on hand at the time the Plan was promulgated (R. 278, 298).

This respondent petitioned the District Court to redistribute the authorized Plan securities no longer required for acquisition of the Junction Bonds (R. 637-40). Such a redistribution would have "sweetened" the assortment of new securities allotted to each class of senior creditors and would have made available, at the bottom of the list, an additional 2¾

million dollars of common stock for allocation to the General Mortgage Bondholders.

The District Court denied the petition saying that it did not believe that it had "the power to make the reallocation requested by the General Mortgage" Trustee. (R. 217).

This respondent appealed from that ruling (R. 650-655) as well as from the confirmation order. The Circuit Court of Appeals agreed with this respondent that the Plan securities originally intended for the Junction Bondholders should be redistributed (R. 250-1).

The Utah Fuel stock.

The Rio Grande Western Railway Company (a predecessor of the Debtor), in 1901 bought all the stock of Utah Fuel Company for $6,000,000 and paid for the stock by putting the stock under the Western Consolidated Mortgage (one of those senior to the General Mortgage) and issuing $6,000,000 of Western Consolidated Bonds to the former owner of the stock (R. 1080, 1097). The Railway Company was entitled to receive back the stock, free of the lien of the Western Consolidated Mortgage, upon payment of $6,000,000 to the trustee of that mortgage.

In 1918, the equity in the stock (then owned by The Denver and Rio Grande Railroad Company, a predecessor of the Debtor) was sold (R. 1082, 1097). Thereafter the Western Pacific acquired title to that equity (R. 1082-3). At that time the Western Pacific and the Missouri Pacific each owned one-half the capital stock of the Debtor (R. 33).

As of December 20, 1924, the Western Pacific and the Debtor entered into an agreement with the Missouri Pacific and James S. Alexander, as trustee,

whereby the Utah Fuel stock was transferred to Alexander, as trustee, still subject, however, to the lien of the Western Consolidated Mortgage (R. 1081-86). By this agreement the Western Pacific assigned to the Missouri Pacific one-half its interest in the Utah Fuel stock "subject to the Consolidated Mortgage, and to the provisions of this agreement". It was then provided that the income from the stock should be paid to the Debtor as long as any of the Debtor's Refunding Mortgage Bonds or General Mortgage Bonds should remain outstanding (R. 1084-86). It was further provided that in the event of the foreclosure of the Refunding Mortgage or of the General Mortgage, the pledged Utah Fuel stock could be sold, still subject to the Western Consolidated Mortgage, and the net proceeds applied to the payment of the Refunding Mortgage Bonds and General Mortgage Bonds (R. 1089-90).

By another agreement, also dated December 20, 1924, the Debtor assigned to the General Mortgage Trustee (*i. e.*, this respondent) and to the trustee of the Refunding Mortgage all of the Debtor's rights and interests "in, to and under" the first agreement of December 20, 1924 (R. 1101).

Thus, in effect, this respondent has had since December 20, 1924, and still has, a junior lien upon the pledged Utah Fuel stock.

The Plan, after providing for the payment of 100% of the claim of the Western Consolidated Bondholders by the issuance of $20,056,400 in new securities of the reorganized Debtor, proposes, in addition thereto, to award to the Western Consolidated Bondholders *all* the stock of the Utah Fuel Company (R. 20-1).

One of the petitioners, Insurance Group Committee, represents owners of about 29% ($4,500,000 principal

amount) of the Western Consolidated Bonds; another of the petitioning group is Guaranty Trust Company as Trustee under the Western Consolidated Mortgage.

The petitioners aver in their brief that the Debtor, at the time of the December 20, 1924 transfer "did not then have, and did not thereby acquire, *any interest* in the Utah Fuel stock"; they note that the Debtor has never recorded that stock on its books but has uniformly carried the 1924 contract at $1. The reason the Debtor avoided technical title perhaps may be found in the so-called Elkins Act, being the "commodities clause" of the Interstate Commerce Act (49 U. S. C. A. Sec. 1 (8)), which, among other things, relates to interstate transportation by a railroad company of commodities manufactured, mined or produced by it or which it may own. That possibility is supported by statements of one of the Debtor's Trustees and counsel for the Debtor's Trustees (R. 1053-4).

Whatever the reason for handling the Utah Fuel stock in the manner above outlined, the statement that the Debtor did not thereby acquire "any interest" goes rather far. The Debtor became entitled to *all dividends* on the stock paid while any of the Debtor's General Mortgage Bonds or Refunding Mortgage Bonds should remain outstanding (except that, in the remote event that the Debtor at any time should have paid all bond interest and all accrued dividends on its preferred stock and appropriated funds to cover such interest and dividends for another year, then as long as that condition should continue, Utah Fuel dividends were to be paid directly to the Debtor's two stockholders) (R. 1085-6). This obligation to pay Utah Fuel dividends to the Debtor was to continue during the period that "any bonds or obligations

issued to pay or refund the General Mortgage Bonds or the Refunding Bonds * * * are outstanding" (R. 1085).

In the depression year 1934, the Debtor received a $250,000 dividend on this stock—a substantial return on an asset valued at one dollar (R. 77)! It is submitted that the practice of carrying contracts, patent rights and other property on the balance sheet at the nominal figure of $1 is not unusual and carries with it no presumption that the asset in question is worthless.

At the approval hearing on September 15, 1943, an officer of Guaranty Trust Company, the present trustee of the Western Consolidated Mortgage, while on the witness stand, agreed that the 1942 net earnings of Utah Fuel Company were about $415,000 and that net earnings for the first six or seven months of 1943 were about $535,000 (R. 1052).*

The Utah Fuel Company owns lands containing estimated reserves of about 112,000,000 tons of coal and in 1935 the daily mine capacity was 6,600 tons (R. 1098).

The testimony relating to the Utah Fuel stock was taken by the Commission in 1937. It is a matter of general knowledge that many coal companies throughout the country were going through dark days in 1935 and 1936. The Commission's 1942 report admits that the Utah Fuel "earnings are not of record since 1936,

* Moody's Manual of Investments—Industrial Securities, 1945 edition, p. 446, shows that total income of Utah Fuel in 1943 was $6,628,846, in 1944 $5,671,979; that net income in 1943 was $865,140, in 1944 $653,904; that earned surplus as of December 31, 1944 was $4,862,980 after listing the capital stock at $10,000,000. In addition there was a small capital surplus. Thus the 1943 figures, which were available to the General Mortgage Bondholders when they voted on the Plan, showed earnings that year of $8.65 per share on the Utah Fuel stock.

in which year, and in 1935, small amounts of net income were reported". All of these figures, of course, represent periods before the construction of one of the world's largest steel plants near Provo, Utah.

Even in 1937, before this development, it was testified by an expert that Utah Fuel during its next 40-year period could have an average expectancy of 1,200,000 tons a year from one part of its mines and 720,000 tons a year from another part, and that it could reasonably expect to have 20% of the total coal business in Utah (R. 811). The same expert testified that the coal properties were "more than ample" for a 40-year period or even a 70-year period (R. 810).

The Circuit Court of Appeals said, in part, with regard to this Utah Fuel stock:

> "There can be no question as to the duty resting upon these claimants [the Western Consolidated Bondholders] to credit the value of this collateral [the Utah Fuel stock] upon their claim before sharing in the securities of the reorganized company. They were entitled only to full payment. If the new securities which were assigned to them satisfied their claim in full, then the plan which permitted them to retain in addition this collateral would be inequitable and unfair to junior creditors.
>
> "The findings of the Commission are not clear as to the manner in which it treated this collateral. * * *
>
> "*Neither does the record establish with any degree of satisfaction the value of this collateral.* There is evidence which would support a conclusion that it had but little value. On the other hand, there is evidence that the Utah Fuel Company is now prosperous and is enjoying large

earnings, with reasonable prospects that they will continue;

"It appears to us that the plan contemplates that the claim of these creditors was to be *satisfied* from the new securities which were set apart for them; and that no particular value was ascribed to this collateral. If this collateral has any substantial value, it must be taken into account before the amount of new securities which are to be set over to these claimants is determined. *The Commission should clear up the doubts and uncertainties which surround this matter* when the proceedings are returned to it for further consideration" (R. 252-3; emphasis supplied).

SUMMARY OF ARGUMENT.

I. The Plan, after its rejection by 79.33% of the General Mortgage Bondholders who voted upon it, may not be confirmed under the provisions of Section 77(e) unless the Court is "satisfied and finds" that the Plan

"makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; affords due recognition to the rights of each class of creditors and stockholders;

does not discriminate unfairly in favor of any class of creditors or stockholders;

will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders;

and "that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts". Any confirmation by the District Court shall be "subject

to the right of judicial review" before it becomes binding on a class of creditors who have rejected the Plan.

The provision for confirmation of a reorganization plan in certain cases notwithstanding the failure to obtain the statutory two-thirds vote of acceptance—sometimes known as the "cram-down" provision—was incorporated into law by the amendments of August 27, 1935. "Arbitrary compulsion" was not intended. The purpose of the amendment was to take away from unreasonable minorities the absolute veto power they had previously possessed. It was intended that the cram-down should be used sparingly.

II. Under the statute the courts have no right to substitute their judgment for that of dissenting bondholders, if the dissenting bondholders have acted in good faith and in the exercise of an honest judgment. If a reasonable business man holding these Bonds could honestly conclude that the Plan was unfair to him, that is the end of the matter. Any other interpretation of the statute would make it a dead letter, and the submission to vote an idle gesture.

III. As the Plan has been construed, it fails to provide for the distribution to creditors of the full amount of the meager capitalization which the Commission found that the reorganized Debtor could properly support. At the same time 90% of the claim of the General Mortgage Bondholders remains unprovided for. For that reason, among others, it would be impossible properly to hold that the rejection was "not reasonably justified".

IV. Up to the end of 1944 there had been impounded for the benefit of the General Mortgage

Bondholders over 9 million dollars of surplus income, over and above full interest requirements of all creditors senior to the General Mortgage Bondholders. Under the Plan the General Mortgage Bondholders are called upon to accept a total of about 4⅓ million dollars of new common stock in full satisfaction of their 43½ million dollar claim.

Although approximately 66⅔% of the General Mortgage Bond interest (or $9,389,418 after full interest on all obligations senior to the General Mortgage Bonds) has been earned during the reorganization period, the Plan calls upon the General Mortgage Bondholders to accept in full satisfaction of their claim for principal and interest, about 12% of the common stock of the reorganized Debtor which, taken at $100 a share, totals only $4,354,816 in aggregate par amount or about 10% of their claim.

This obvious inequity does not permit the conclusion that the rejection vote was "not reasonably justified".

V. The Plan allots to some of the senior creditors, in addition to 100% of their total claim in new securities of the reorganized company, all of the outstanding 100,000 shares of Utah Fuel stock, upon which the General Mortgage Bondholders have a junior lien. That has been done in complete disregard of the rights of the General Mortgage Bondholders, without any determination as to the value of the Utah Fuel stock, although it seems obvious that such value is substantial. With such a serious shortcoming in the Plan, it would not be proper to hold its rejection "not reasonably justified".

VI. No plan at any time proposed by the senior creditors provided less than 47.42% treatment for the

General Mortgage Bonds; until July 27, 1942, no plan proposed by anyone provided that the General Mortgage Bonds should receive less than approximately one-third of their total claim in new stock. Thus, the senior creditors have admitted that the General Mortgage Bondholders are entitled to better treatment. The Commission has nowhere satisfactorily explained or justified the change from the 50% and 33⅓% treatment proposed in its first four plans to the 5% and 10% treatment proposed by it in 1942 and 1943.

The General Mortgage Bondholders have been presented with a paradoxical situation. During a period when the railroad is enjoying the greatest prosperity in its history, the General Mortgage Bondholders have been asked to accept the most drastic sacrifice ever suggested for them. It is that proposal which is "not reasonably justified", rather than the rejection of that proposal.

VII. All three judges of the Circuit Court of Appeals have held unanimously that the Plan is not fair and equitable. Even the District Court, which undertook to confirm the Plan over the rejection vote, indicated that it had some reluctance about doing so. The House Judiciary Committee was unanimously of the opinion that the Plan imposed "an unbearable hardship upon the junior investors". In the light of the foregoing, it cannot properly be held that the General Mortgage Bondholders were "not reasonably justified" in rejecting the Plan.

VIII. The General Mortgage Trustee offered the expert testimony of two admittedly well-qualified witnesses, Miles C. Kennedy and Ralph E. Morton, to the effect that in their opinion the rejection vote

was reasonably justified in the light of all the relevant facts. No testimony evidencing a contrary opinion was offered.

IX. Although it seems too clear for serious argument that the rejection vote in this case was not of an unreasonable type which the courts may properly override, it is also the fact that any confirmation of a reorganization plan under Section 77 in a case where the plan has failed to get the approval of even a bare majority of those voting of a class of creditors entitled to vote would be an unprecedented extension of the bankruptcy power. It would eliminate the line of reasoning followed by this Court in the *Rock Island* case in sustaining the constitutionality of Section 77.

X. The General Mortgage Trustee at no time has made any claim that the General Mortgage Bondholders should receive any of the surplus cash or any of the senior securities which have been "released" through the elimination of the Junction Bonds or which may become available through payment of the Chase note, reduction of any other senior claim, more appropriate treatment of the Utah Fuel stock, or otherwise. Far from being startled into saying that "the Circuit Court does not mean what it says" (petitioners' brief 54), this respondent observes that the Circuit Court does not mean what *the petitioners say* it says. A fair reading of the opinion below fails to disclose any requirement or direction that cash or senior securities be "distributed" to the General Mortgage Bondholders. Statements to that effect (petitioners' brief 32-33, 53, 54, 55, 87) are incorrect. The court below recognized that any distribution of cash or securities would be made to the

"various classes of creditors according to their priority in rank" (R. 246). When such a distribution or redistribution is made the senior creditors will receive in appropriate proportions securities of higher grade than offered them in the Plan. The common stock no longer needed for the senior creditors will then be available for distribution to the General Mortgage Bondholders.

ARGUMENT.

I.

The purpose of the August 27, 1935 amendments.

That part of Section 77(e) of the Bankruptcy Act which is here applicable provides that the Court, under certain carefully specified conditions, may confirm a plan which has failed to receive the statutory two-thirds vote of acceptance.

It is obvious that the intent of Congress in adding to Section 77 this so-called cram-down provision was to prevent selfish and unreasonable minorities from staging a hold-up, and to make it impossible for such minorities to take advantage of their nuisance value to drive an unconscionable bargain.

This seems clear enough, and for that reason any reference to the proceedings in Congress at the time of the adoption of the amendments may be superfluous, but in the appendix to this brief are excerpts from the committee reports and statements of those in charge of the bill in both Houses of Congress—which confirm what is said above regarding the intent and purpose of the provision (Appendix 12-32).

Sen. Rep. No. 1236 refers to the "obstructive possi-

bilities" in the *Missouri Pacific* case, with "72 different classes of security holders" and "one bank loan from J. P. Morgan & Co. * * * in a separate class" (Appendix 20).

Representative Summers, who was the judiciary committee member in charge of the bill in the House, in the course of the debate on the proposed amendment also referred to the *Missouri Pacific* case and its "72 classes" (Appendix 22), and Senator Wheeler, in charge of the bill in the Senate, in turn, mentioned the Missouri Pacific's 72 classes and the bank loan of J. P. Morgan & Co., separately classified, making it "impossible to get through a plan without either meeting the Morgan's terms or paying the value of their interest in cash" (Appendix 26).

Senator Hastings of the same committee also pointed to the 72 classes and to the possibility of "some man or some few people standing out, demanding 100 percent payment of their claims" (Appendix 29).

It obviously was the intent of Congress, as evidenced in the debates and reports on the bill, that the cramdown provision should be used sparingly. In the January 21, 1935 report of Joseph B. Eastman, Federal Coordinator of Transportation, on which the amendatory bill was based, Mr. Eastman stated (Appendix 13):

> "Arbitrary compulsion of plans over the dissents of the interested classes is not intended, nor is it believed that the courts will override strong dissents by any large number of such classes, or by a single large class, excepting where it is established that they have no interest in the property. Rather, the purpose is to prevent the obstruction of plans which are favored by the

larger classes of creditors or shareholders, but which are obstructed by minorities in the smaller classes in the attempt to secure unduly preferential treatment. * * *"

Senator Hastings stressed the protection given dissenting security holders by the provisions for appeal pointing out that the "court, of course, will go a long way before agreeing to that [the cram-down] if there be a real controversy" (Appendix 30) and that there was always "the right of appeal if the court dealt unfairly with them". Senator Wheeler mentioned the "double check" provided by the Commission and the Court, and Senator Hastings agreed, adding "there is a right of appeal to the circuit court from the decision of either of them" (Appendix 31).

It is also interesting to note that the same amendments were also intended "to protect the stockholders and creditors against unnecessary sacrifice" (Appendix 17, 21, 22-3, 24, 28). It was hoped to accomplish this through the so-called "rain check" provision of the bill. In commenting upon it, Representative Michener of the Judiciary Committee said:

"* * *. It guarantees to the last equity holder every possible chance to realize on his investment if business does pick up and the railroads again become profitable" (Appendix 24).

and Senator Wheeler reported:

"In a recent reorganization of an industrial concern many of the stockholders were completely wiped out. They were given no new stock. They received nothing at all.

"Then after reorganization business began to pick up because of more prosperous conditions,

but these stockholders who had invested their money remained completely wiped out, while other investors reaped the reward. This so-called 'rain check' device is to protect that class of stockholders" (Appendix 28).

II.

If a reasonable business man could honestly conclude that the Plan was unfair, the statute does not give the Courts power to override the rejection vote.

The petitioners erroneously assert that the Circuit Court of Appeals held that "the dissent of the General Mortgage Bondholders precludes confirmation of the Plan" (petitioners' brief 36, 100-106). An examination of the opinion below will show that it contains no such holding. The Circuit Court of Appeals pointed out numerous respects in which it found that the Plan was *inequitable* and *unfair* and *did not comply with the requirements of Section 77(e)* and *then* held: "It follows from what has been said that the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, * * *" (R. 253). The Court decided, first, that because the Plan was not fair and equitable, the rejection vote was reasonably justified; and, secondly, that, because the Plan was not fair and equitable *and* because the rejection vote was reasonably justified, the District Court erred in confirming the plan (R. 253). That is very far removed indeed from a holding that a rejection vote "precludes" confirmation.

Under the statute, of course, a plan may not even be submitted to creditors for a vote until the District Court has held that it is fair and equitable. If the District Court's determination that the Plan is fair

and equitable were final, all of the statutory provisions for submission would be meaningless surplusage. In that event, the careful canvassing, supervision and tabulation of the vote by the Commission (R. 265-274) would be an indefensible waste of time and money. The fact would be that the Courts, the Commission and the creditors have been "shadow-boxing" since October 25, 1943—the "approved" date on which the District Court made that very determination—permitting the submission to creditors for a vote.

Clearly, the Congress cannot be presumed to have intended such futile procedure. The statute must mean what it says. The rejection vote may not be set aside unless it is determined affirmatively (and the District Court's decision is affirmed on appeal, if judicial review is requested) that the rejection was "not reasonably justified".

It should be noted that those rejecting the Plan are *not* required to establish that their action was "reasonably justified". The burden of proof is just the other way. Those who wish the Court to confirm the Plan notwithstanding its rejection must show by persuasive evidence, and by a preponderance of the evidence, that the rejection vote was not reasonably justified within the meaning of the statute. The supporters of the Plan completely failed to maintain that burden. On the contrary, the record affirmatively shows that the rejection vote was "reasonably justified" within the meaning of the statute.

If any reasonable business man could honestly have come to the conclusion the General Mortgage Bondholders reached, the rejection vote may not be set aside. Any other interpretation of the statute would make it a dead letter.

Under the statute the final safeguard is supplied

by requiring acceptance of the proposed composition by the creditors whose investment is at stake. Unless their action is not reasonably justified, their judgment controls.

The courts should not undertake to substitute their judgment for that of creditors, except under conditions indicating clearly that the creditors acted from improper motives or in an unreasonable, arbitrary or capricious manner. No such conditions here exist.

III.

As the Plan has been construed it fails to distribute completely the full amount of authorized securities which the Commission held that the reorganized Debtor could properly support.

As set forth in the Statement, the Plan as promulgated by the Commission provided for the issuance of $2,123,916 of new first mortgage bonds and $634,417 of new income bonds in exchange for the Junction Bonds. After the date of the Plan there was a substantial improvement in the Debtor's cash position and its net working capital. Mr. Thompson testified that on January 1, 1943, the proposed effective date of the Plan, the Debtor's Trustees had on hand cash and government bonds aggregating $10,850,000 (R. 278) and that on September 16, 1943 the total was approximately $20,000,000 (R. 278).

At a court hearing on September 14, 1943, the District Court ordered the payment or purchase of the Junction Bonds by the application of this "surplus cash" (R. 262-3).

After most of the Junction Bonds had been acquired by the Debtor's Trustees, the General Mortgage Trustee petitioned the Court for a redistribution of

those authorized securities which would no longer be required for issuance in exchange for the Junction Bonds (R. 637-640). It pointed to the provision of the Plan which it thought authorized such a redistribution and cited similar redistributions in other pending reorganization cases. The District Court, however, concluded that it did not have the power to make the redistribution or reallocation requested (R. 217).

As a result of that interpretation of the Plan it now appears that if the Plan were to be confirmed there would be outstanding approximately $2\frac{3}{4}$ million dollars less of authorized securities than was contemplated by the Commission. The reorganized Debtor will possess all of the property which the Commission determined would support the issuance of these new senior securities. It will have all the cash and all the working capital which the Commission deemed appropriate to sustain the operation of the reorganized Debtor. The Junction Bonds have not been "excluded", as suggested by the petitioners. They have been definitely included. They have been acquired by the Debtor's Trustees from surplus cash accumulated since the effective date of the Plan. They no longer remain outstanding as an unsatisfied lien upon the Junction property—which would be the only excuse for holding unissued the new first mortgage bonds and new income bonds in the Plan dedicated to the discharge of that lien.

If the $2\frac{3}{4}$ million dollars of authorized securities were not "redistributed", as prayed by this respondent and as the Circuit Court of Appeals indicates should be done (R. 250-1), the net result would be that the authorized capitalization of the reorganized company would be *decreased* by that amount—although

there has been no corresponding decrease in its earning capacity.

Under these circumstances the Plan as interpreted deals unnecessarily harshly with the General Mortgage Bondholders, 90% of whose claim is being forever wiped out. Their action in rejecting such a plan cannot properly be said to have been "not reasonably justified" within the meaning of the statute.

This feature of the Plan, as interpreted by the District Court, also clearly shows that the Plan fails to measure up to the requirements of Section 77(e).

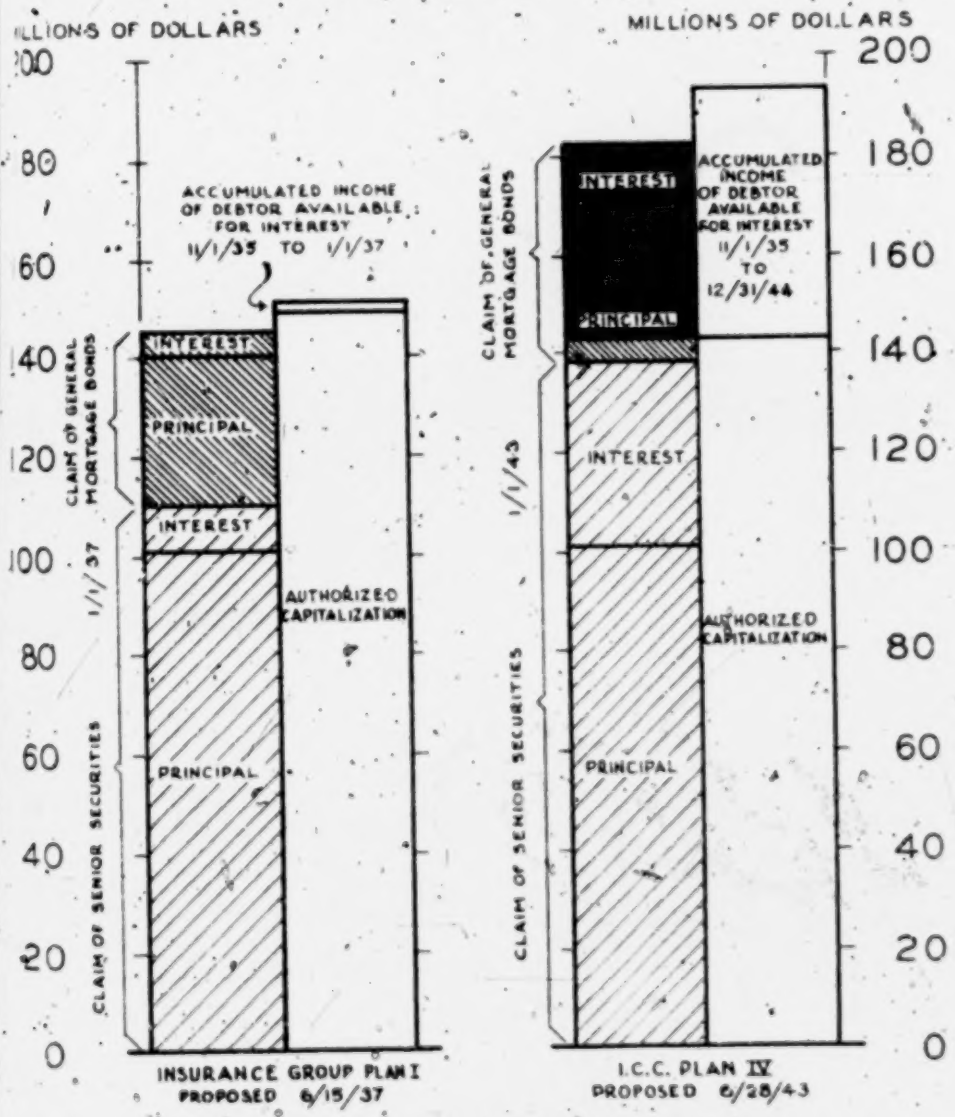
IV.

After the impounding for their benefit of over 9 million dollars of surplus income, the General Mortgage Bondholders were not acting unreasonably in rejecting a Plan giving them about 4⅓ million dollars of new stock in full satisfaction of their $43,548,155 claim.

The table on page 18 of this brief shows that up to the end of 1944 the Debtor's income had exceeded the interest requirements of all securities senior to the General Mortgage Bonds by $9,389,418. This is equal to about one million dollars a year available for application to payment of interest on the General Mortgage Bonds. Shortly after these reorganization proceedings started the General Mortgage Trustee made proper demand for the impounding of all net income from the mortgaged property for the benefit of the General Mortgage Bondholders (R. 376-398).

The supporters of the present Plan admitted in 1937 that the General Mortgage Bondholders were entitled then to receive 100% of their claim in new common stock, by proposing a plan which so pro-

TREATMENT OF GENERAL MORTGAGE CLAIM UNDER (1) INSURANCE GROUP PLAN OF 1937, AND (2) PLAN NOW UNDER CONSIDERATION



CLAIM OF SENIOR CREDITORS FOR WHICH NEW SECURITIES ARE PROVIDED.

CLAIM (OR PORTION OF CLAIM) OF GENERAL MORTGAGE BONDHOLDERS FOR WHICH NEW SECURITIES ARE PROVIDED

PORTION OF CLAIM OF GENERAL MORTGAGE BONDHOLDERS WIPED OUT

NOTE: AS OF 12/31/44 CLAIM OF SENIOR SECURITIES INCREASED BY $8.9 MILLIONS (ACCRUED INTEREST) AND DECREASED BY $4.0 MILLIONS (DEBT RETIREMENT) OVER AMOUNTS SHOWN WITH RESPECT TO I.C.C. PLAN IV

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, DEBTOR

the end of 1944, notwithstanding the accumulations of earnings substantially greater than the accumulation of unpaid interest on the claims of the senior creditors, the General Mortgage Bondholders, under a proposed capitalization of $143,528,027 have been almost shoved out of the picture by the interest accumulation on the senior debt, although that interest was earned with over $9,000,000 to spare.

Interest at the contract rate of 5% on $29,808,000 of General Mortgage Bonds amounts to $1,490,400 per year. Accordingly, during the reorganization period, over two-thirds of the interest, at the original contract rate, has been earned on all the outstanding General Mortgage Bonds. Involved in this nine-year period are the six worst years ever recorded for this Debtor (R. 348).

In the face of these facts, the Plan requires the General Mortgage Bondholders forever to forego 90% of their claim—to accept $4,354,816 of new common stock in full satisfaction. Obviously, their rejection of such a harsh and inequitable proposal cannot be set aside as "not reasonably justified".

V.

Because of the "bonus" to senior creditors of the Utah Fuel stock, on which the General Mortgage has a lien, the rejection vote cannot be held unreasonable.

The Plan provides that certain senior creditors, the holders of the Western Consolidated Bonds, shall receive 100% of their 20-million-dollar claim in new securities of the reorganized Debtor (R. 183). It also provides that these creditors shall receive all of the pledged Utah Fuel stock (R. 204, 167). The

pertinent facts regarding the Utah Fuel stock are set forth in the Statement. The 100,000 shares involved constitute all the outstanding stock of this corporation, which has no funded debt (R. 1110A).

The Circuit Court of Appeals says that it "appears to us that the plan contemplates that the claim of these creditors [the Western Consolidated Bondholders] was to be *satisfied* from the new securities [the securities of the reorganized Debtor] which were set apart for them, and that no particular value was ascribed to this collateral [the Utah Fuel stock]" (R. 253). That is a fair inference from the Plan language.

The Circuit Court of Appeals also held that the record does not "establish with any degree of satisfaction the value of this collateral" (R. 253).

The General Mortgage Bondholders, who are to receive only 10% of their claim under the Plan (R. 183), have a junior lien on the Utah Fuel stock, as well as certain other rights with respect thereto (this brief 26-31), and are entitled to share the benefit of that collateral after senior liens have been satisfied.

If the Utah Fuel Stock is now worth $20,000,000 as is not improbable, it is approximately equal in value to the entire claim of the Western Consolidated Bondholders, principal and accrued interest to the Plan's effective date, which totals $20,456,400 (R. 183). In other words, the allocation of the Utah Fuel stock, free and clear of the General Mortgage lien, to these senior creditors would approximately satisfy their claim. Under the Plan, however, they are to receive, in addition, $20,456,400 of assorted securities of the reorganized Debtor.

The petitioners seek to dispose of this troublesome

defect in the Plan by asserting that "Since the Utah Fuel stock is not property of the Debtor, it is not subject to disposition under Section 77 * * *". They admit that "* * * of course the Western Consolidated bondholders may not obtain a total realization, measured by actual value, that exceeds the amount of their claim". The petitioners assert that "* * * when enforcement of the pledge by distribution or sale is sought, * * * it will be appropriate in *those proceedings* to inquire whether such action will result in any excess realization" and that "Full protection can *then* be given to all those who have any junior interest in the stock" (petitioners' brief 94, 95).

Just how the junior lien of the General Mortgage Bondholders on this Utah Fuel stock is to be protected the petitioners do not make clear. Under the Plan the General Mortgage Bondholders are required to surrender their bonds for new common stock equal to 10% of their claim. Presumably the General Mortgage then goes out of existence. The new common stock is to be distributed to six different classes of creditors so that many of the holders of the new common stock will not be entitled to the protection of this junior lien on the Utah Fuel stock. It is the undisputed fact that the Western Consolidated Bondholders have a lien, limited to .6 million dollars in total amount, upon the Utah Fuel stock and everything over and above that amount stands as security for the Refunding Bonds and the General Mortgage Bonds. The Refunding Mortgage admittedly has a prior lien on all property covered by the General Mortgage. The Commission, by allowing the General Mortgage Bondholders to participate in the securities of the reorganized Debtor, has by that very fact determined that the Refunding Mortgage Bondholders are

already given all to which they are entitled. Accordingly the benefit of any surplus value over and above the amount required to satisfy the claim of the Western Consolidated Bondholders, clearly should go to the General Mortgage Bondholders.

It is submitted that if various classes of creditors of the Debtor have different rights and interests in the Utah Fuel stock, those rights should have been considered in the preparation of the Plan, and that these creditors should not immediately after consummation of the Debtor's reorganization be forced back into court for adjudication of their rights—merely on the theory that the Debtor does not have "any interest" in this stock.

Moreover the petitioners seem to overlook the provisions of the above-mentioned agreement of December 20, 1924 to the effect that in the event of foreclosure, if the trustee under the General Mortgage requests the sale of the Utah Fuel stock "such sale of the Utah Fuel Stock and application of the proceeds thereof shall be made *before the application to such payment of the property subject to such mortgages [meaning the Refunding Mortgage or the General Mortgage]*, or other indentures, or the proceeds thereof" (R. 1090; emphasis supplied).

Were this Plan to be consummated, the right of the General Mortgage Bondholders to participate in the security afforded by the Utah Fuel stock would be destroyed—and, in view of the rejection vote, clearly without their consent.

The petitioners cite the *Western Pacific* case* and erroneously argue that the claim of the Railroad

* *Ecker v. Western Pacific R. Corp.* (1943), 318 U. S. 448, 87 L. Ed. 892.

Credit Corporation there was handled similarly to the proposed treatment of the Utah Fuel stock. In the *Western Pacific* case the collateral was pledged by a third party; in our case it was pledged by the Debtor's predecessor. In the *Western Pacific* case no bond issues had any lien on the collateral; in our case three bond issues, including the General Mortgage, have a lien. In the *Western Pacific* case the accommodation collateral was not awarded to the Railroad Credit Corporation or to anyone else (rights were left unaffected); in our *Denver* case the pledged Utah Fuel stock is to be distributed exclusively among the holders of the Western Consolidated bonds (R. 20). No analogy exists.

The Circuit Court of Appeals has held that the "Commission should clear up the doubts and uncertainties which surround this matter" (R. 253).

The Plan treatment of the Utah Fuel stock, coupled with the inadequacy of the Commission's report with respect to (a) the value of the stock and (b) the theory upon which it was handed over to the senior creditors, free of any duty to account to the junior lienors, establishes with abundant clarity that the rejection vote was not unreasonable.

VI.

The senior creditors have admitted that the General Mortgage Bondholders are entitled to better treatment.

The treatment proposed for the General Mortgage Bondholders in eleven different plans is tabulated in the Statement (this brief 9), and is shown graphically on the charts opposite pages 12 and 19. Three

of these plans were proposed by the senior creditors, providing the following treatment for our Bonds:

Plan	General Mortgage Treatment
Insurance Group I	100%
Discussion	50%
Insurance Group II	47.42%

The sequence of the plans is also significant. At the outset the Insurance Group had no question but that the General Mortgage Bondholders should receive 100% of their total claim and, in fact, their 1937 plan gave these bondholders Class A common stock in that amount. Thereafter, in 1938-39-40, the Commission and its Examiner proposed three plans. In the first of these 50% treatment was provided for the General Mortgage Bonds and the other two reduced that percentage to 33⅓%. Promptly thereafter the senior creditors joined in putting forward the so-called Discussion plan, filed January 6, 1941, which brought back the General Mortgage treatment to 50%. It should be noted that the institutions which compose the group of senior creditors hold absolutely none of the General Mortgage Bonds and obviously would not have suggested increasing the allotment for the General Mortgage unless satisfied that this was demanded by considerations of equity and fairness.

In September of 1941 the Commission's Examiner made a new proposal, dropping the General Mortgage Bondholders to the same 33⅓% treatment previously proposed by the Commission. About a month after that, the Insurance Group Committee again came back with a counter-proposal, this time raising the General Mortgage treatment to 47.42%. That is the minimum treatment ever proposed for the General Mortgage Bonds by the senior creditors.

We cannot assume that the representatives of the

senior creditors proposed giving away to the General Mortgage any of the equity rightfully belonging to the bondholders they represented. The only proper inference to be derived from their successive proposals of 100%, then 50%, then 47.42%, for the General Mortgage Bonds is that they honestly were of the opinion that these percentages represented the least to which the junior bondholders were entitled. Unless they were satisfied as to this, it is apparent they would have been content to leave the General Mortgage Bonds with the treatment last previously proposed by the Commission. Obviously they were convinced that the Commission had dealt entirely too harshly with the General Mortgage.

Turning from the three plans proposed by the senior creditors to the six plans proposed by the Commission, the facts are as follows (see table, this brief 9):

Plan	General Mortgage treatment
Examiner's I	50%
ICC I	33⅓%
ICC II	33⅓%
Examiner's II	33⅓%
ICC III	5%
ICC IV	10%

Thus, the Commission and its Examiner in four successive plans, proposed in four successive years, consistently provided at least 33⅓% treatment for this bond issue. No one in the proceedings, no adverse party, had even suggested the possible desirability of making any reduction in the treatment of the General Mortgage Bonds. As already stated, the other parties had proposed just the opposite. The Commission made this drastic cut in 1942 and 1943, to 5% and 10%, of its own motion. It has not justified the change. It is submitted that the change cannot be justified.

The Commission held in 1943 that the Debtor's property would support a capitalization of $143,528,027 (R. 159, 184). In 1939 and 1940 it had held that the property would support a capitalization of about 135 million dollars (R. 352, 98-112). In the years 1941-43, plus the first seven months of 1944,* over 30 million dollars were spent on additions and betterments, over and above normal maintenance. Of this amount over 27½ million dollars were charged to capital account.

It would seem reasonable to assume that these additions and betterments would permit an increase in the capitalization, which the property could support, commensurate with the expenditures. Yet the Commission allowed an increase of only about 7¾ million dollars, or less than one-third the amount spent. This reflects no great confidence in the wisdom of these expenditures. The fact is, however, that the expenditures have greatly improved the earning capacity of the railroad as amply demonstrated by the operating results of more recent years.

It must be kept in mind, in this connection, that the income available for interest in 1942, when the first of these confiscatory plans was proposed, was $17,180,067,** and in 1943, when the other was proposed (the plan now under consideration), the income available for interest was $11,766,711.** The earnings during these two years were the highest thus far, during the reorganization period. In contrast, in 1939 (when the Commission proposed its first plan) it observed that the reorganization should not be "sub-

* These were the latest figures before the District Court at the hearing on confirmation. The amounts have increased substantially since then.

** These figures taken from tables on page 18 of this brief and were obtained as there explained. The 1943 Annual Report, p. 11 gives slightly different figures: for 1942—$17,044,420.39; for 1943—$11,573,667.94.

jected to undue delay pending a demonstration that the carriers can again earn more than $3,000,000 a year" (R. 67).

The Commission's second supplemental report of July 13, 1942, contains a statement that "The trend of earnings indicates that in 1942 the debtors' forecast for a future normal year, showing an available income of $6,215,423 will be exceeded" (R. 124). That was at least an understatement in view of the actual figure of $17,180,067 (this brief 18). The same report carefully made provision for a $2,250,000 note to the R. F. C. for "new money" (R. 145).

In its June 14, 1943 report the Commission noted the 1942 earnings figures, as well as the figures for the first two months of 1943, and as a result, "eliminated, as an item of the new capital structure" the 2¼-million-dollar note for "new money" (R. 155-6). The Commission still included provisions, however, for new borrowing from the R. F. C. in an amount up to $2,000,000 in connection with the reorganization and, in the alternative, for the issuance of an additional $2,250,000* of new first mortgage bonds (R. 156).

The 1942 and 1943 plans provided for substantially the same authorized capitalization (this brief 9; R. 183, 355), which was only about 7¾ million dollars more than the lowest capitalization ever suggested for this Debtor—that proposed in July 1939 after the worst 4½ years recorded for this property (R. 348).

The record shows that there is a substantial prospect of this railroad earning enough to enable the General Mortgage Bondholders to recoup all of their investment. A fair and equitable plan would give them such an opportunity. Giving them common stock would add nothing to the fixed charges, and in no way jeopardize the road's financial stability, yet would

* The Plan itself gives this figure at $2,500,000 (R. 23).

give them the benefit of earnings in excess of those necessary to cover the securities allocated to senior creditors. The Plan denies them that chance.

The fact of the matter is that the General Mortgage Bondholders were lost sight of, or disregarded. They were caught in a squeeze. The table on page 9 of this brief shows that the authorized capitalization in all the plans did not fluctuate greatly. This is shown graphically at the top of the chart which appears opposite page 42. Thus the ceiling remained fairly constant above them. Beneath them, however, there was a steadily rising floor representing the claim of the senior creditors, including accrued unpaid interest. Just how this floor rose can be shown by comparing the principal of the senior claims* with the total claims, principal plus interest, to January 1, 1943, provided for in the Plan (R. 183):

Description of Senior Debt	Principal of senior claims December 31, 1935	Claims principal plus interest to Jan. 1, 1943
R. G. West. First Trust 4's	$ 15,150,000	$ 20,050,800
R. G. West. Cons. 4's	15,089,000	20,056,490
R. G. June. First 5's	2,000,000	2,758,333
D. & R. G. Consol. 4's	34,125,000	45,727,500
D. & R. G. Consol. 4½'s	6,382,000	8,823,115
Refunding & Impt. 5's	12,000,000	16,950,000
Refunding & Impt. 6's	2,000,000	2,990,000
Chase National Bank Note	1,500,000	2,158,458
R. F. C. Notes	10,691,850	12,900,605
Equipment obligations	2,325,000	5,758,000†
TOTALS	$101,293,850	$139,173,211

* 1935 Annual Report, pp. 13, 14.

† The increase in equipment obligations is due to money borrowed by Trustees for purchase of *new* equipment and for *improvements* in the Debtor's property, *not* accumulated interest. This amount is included in the tabulation because the Commission allows this new debt (representing *part only* of the value of *new* equipment and of *new* additions and betterments now belonging to the Debtor) to combine with the accumulated interest on the senior debt in squeezing out the General Mortgage Bondholders.

Thus, during that period there was an increase in the total of claims senior to the General Mortgage Bonds amounting to $37,879,361. That increase is approximately equal to the face amount of claim which the General Mortgage Bondholders under the Plan are asked to give up, $39,193,339.

During the reorganization, through July 31, 1944, the last month-end prior to the confirmation hearing, the Debtor's Trustees had spent over $54,373,238 for improvement of the Debtor's property over and above normal maintenance, of which $43,291,513 was charged to capital account in accordance with the rules and regulations of the Commission (table, this brief 13).

There was no corresponding increase in authorized capitalization.

The above facts account for the "squeeze" just mentioned. There was a constantly shrinking margin between (a) the total amount of authorized securities, available for distribution to all creditors, on the one hand, and (b) the total amount of the senior claims, on the other. At the outset the margin was wide enough to accommodate the entire claim of the General Mortgage Bondholders. Under the Plan the margin had shrunk to such an extent that 90% of the General Mortgage claim had been squeezed out.

Elsewhere, we discuss the elimination, through the use of surplus cash earned after the promulgation of the Plan, of the Junction Bonds. As a result of the payment or purchase of the Junction Bonds the "steadily rising floor" should be at least $2,758,333 lower because at least that amount of the senior claims no longer need be provided for out of the authorized securities, but that adjustment has not been made.

If the Utah Fuel stock is properly valued and

handled, as discussed previously, perhaps the "floor" may be lowered another 10 or 15 million dollars.

Looking at this sequence of events from the point of view of a General Mortgage Bondholder, the situation appears a Gilbertian paradox. Here were eleven successive plans. The first five were proposed in years in which the earnings were poor—not even sufficient to cover the senior bond interest. These five plans proposed giving the General Mortgage Bondholders a substantial part of their claim in new securities, the several percentages being 100%, 100%, 50%, 33⅓%, and 33⅓%.

In contrast came six later plans, all of which were proposed in years of substantially better earnings—in every one of which all senior bond interest was earned. Only one of these six plans (the Discussion plan) suggested as much as 50% treatment for the General Mortgage. The last two plans, proposed during years of maximum prosperity (to date), dropped the luckless General Mortgage Bondholders to 5% and 10%, respectively.

The paradox is shown in tabular form in the Statement (this brief 11), and more graphically by the charts opposite pages 12 and 19.

What made it even more difficult for a General Mortgage Bondholder to understand the sequence was the fact that no security holder, at any time, ever suggested that the General Mortgage Bondholders were given too favorable treatment in any proposed plan. On the contrary, the other parties consistently proposed improving the treatment of the General Mortgage.

With the enormous earnings prevailing in 1942 and 1943, the unexpectedly drastic cut in the allotment provided for the General Mortgage in the Commission's last two plans appeared completely unreasonable to a

General Mortgage Bondholder; and, when he voted, in 1944, the railroad was having another banner year.

With that background, it seems self-evident that the action of the General Mortgage Bondholders in rejecting the Plan was not unreasonable.

VII.

In the light of the views expressed by the Circuit Court of Appeals, by the District Court, and by the unanimous House Judiciary Committee, it cannot properly be held that the General Mortgage Bondholders were "not reasonably justified" in rejecting the Plan.

For various reasons set forth in its opinion, the Circuit Court of Appeals found that the Plan "is inherently inequitable and unfair" (R. 247), that it has an "inherent weakness" (R. 248), that the General Mortgage Bondholders "have a real grievance" (R. 248), that the Plan "does not comply with the requirements of Section 77(e)" (R. 251), and that the Plan "fails to meet the requirements" of that Section (R. 253).

The District Court itself, in the very opinion which overrode the rejection vote of the General Mortgage Bondholders and confirmed the Plan notwithstanding its rejection, indicated that it had some reluctance in the matter. It pointed out that it had previously itself put forward a plan giving the General Mortgage Bondholders a larger amount of common stock but that it had been overruled by the Commission. The District Court felt that it would be "a useless gesture" for it to do the same thing again. As if interpreted the decision of this Court in the *Milwaukee* case* it

**Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific Railroad Co.* (1943), 318 U. S. 523, 87 L. Ed. 859.

apparently felt that it was forced to go along with the Commission. The District Court said (R. 221):

> "The court, in its plan of March 6, 1941 gave the General Mortgage bondholders more common stock than does the approved plan. The Commission, however, could not agree with our views, and it would seem to be a useless gesture for the court to make the same error again assuming we had the power."

Extracts from an unanimous report of the House Judiciary Committee (78th Cong., 2d Sess., Rep. No. 1615), recommending the passage of H. R. 4960, are included in a footnote to the concurring opinion of Circuit Judge Phillips (R. 255-9). That report referred specifically to our *Denver* case, pointing out that in 1942 the Denver & Rio Grande system earned $34.40 a share on its common stock (after all prior charges) and that the same figures were repeated approximately in 1943 and were continuing in 1944. The report stated: "That this situation has created an unbearable hardship on the junior investors in railroad securities * * * may be easily seen * * *."

It seems clear from this and other language of the unanimous report that the members of the Judiciary Committee did not consider the Plan fair and equitable and, if called upon to vote on the Plan, would have rejected it.

The petitioners would have this Court rule that the General Mortgage Bondholders whose views about the Plan apparently coincide with the unanimous Circuit Court of Appeals and with the unanimous House Judiciary Committee were "not reasonably justified" in holding those views and in voting, accordingly, to reject the Plan.

VIII.

The rejection vote was "reasonably justified" in the opinion of the only witnesses called to give expert testimony.

At the hearing before the District Court on the confirmation of the Plan, the significance of many uncontroverted facts, discussed earlier in this brief, with respect to the vital question of whether or not the rejection vote was one that could properly be overridden as "not reasonably justified" was covered by the expert testimony of the witness, Miles C. Kennedy.

Mr. Kennedy is a member of the consulting engineering firm of Coverdale & Colpitts. The District Court and counsel for the Insurance Group Committee and the R. F. C. waived all testimony offered as to the qualification of this witness and conceded that Mr. Kennedy and his firm have in a very large number of railroad reorganization cases served as special advisors to bondholders, bondholders' committees, creditors' groups, and the like. All conceded Mr. Kennedy's expert professional experience and qualifications.

The significance of Mr. Kennedy's testimony best appears from an examination of it in its entirety (R. 310-334). For the convenience of the Circuit Court of Appeals, an abstract of part of Mr. Kennedy's testimony was prepared and it has been reprinted in the appendix to this brief (Appendix 1-8).

Mr. Kennedy's testimony was supplemented by that of the witness, Ralph E. Morton, a vice president of City Bank Farmers Trust Company, the trustee under the General Mortgage (R. 335-342). An abstract of

part of Mr. Morton's testimony is printed in the appendix (Appendix 9-11).

After extended preparation, the respective expert opinions of these witnesses was asked on whether the rejection vote was "reasonably justified in the light of all the relevant facts". The District Court received an opinion from Mr. Kennedy that the rejection was reasonably justified (R. 319-20; Appendix 6-7), but sustained an objection to an opinion to the same effect from Mr. Morton (R. 335; Appendix 11).

IX.

Confirmation of a Plan which has failed to get even a bare majority approval would be an unprecedented extension of the bankruptcy power.

The contention of the senior creditors that this Plan should be crammed down the throats of the General Mortgage Bondholders after they have rejected it by a vote of 4 to 1 and after a unanimous Circuit Court of Appeals has held that the Plan is unfair and inequitable as to them, raises a serious constitutional question. Forcing such a plan upon holders of bonds, secured by a duly recorded mortgage, involves the confiscation of property rights of the highest type. We are dealing with railroad mortgage bonds, a type of security in which the public has been accustomed to invest its savings.

The confirmation of the Plan would involve confirming a plan which not only has failed to obtain the two-thirds vote of acceptance prescribed in Section 77 (e) as amended, but *also has failed to obtain even the approval of a majority of the General Mortgage Bondholders voting.*

Counsel for the Insurance Group insist that it is no longer possible to challenge the constitutionality of Section 77 and cite the comprehensive analysis of that statute by this Court in the *Rock Island* case,* in which the constitutionality of Section 77 was sustained.

Section 77 was amended in a very important respect after the date of that decision. The later amendment took from the statute the very provision on which this Court heavily relied in sustaining the statute's constitutionality.

In the *Rock Island* case this Court, in passing upon the constitutionality question, pointed out that, under the statute as it then stood,

> "No plan may be finally approved by the Commission until it has been accepted in writing by or on behalf of creditors holding two-thirds in amount of the claims of each class affected by the plan * * *." (294 U. S. 663)

and that

> "Upon confirmation of the plan, it is to be binding not only upon corporation and all stockholders and creditors generally, but upon all secured creditors of each class of which two-thirds in amount shall have accepted the plan." (p. 663)

After referring to Article I, Section 8, Clause 4, of the Constitution, which vests Congress with the power to establish bankruptcy laws (p. 667), this Court reviewed their development (pp. 667-675), and said:

> "But, while it is true that the power of Congress under the bankruptcy clause is not to be limited

* *Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Railway Co.* (1935), 294 U. S. 648, 55 Sup. Ct. 595, 79 L. Ed. 1110.

> by the English or Colonial law in force when the Constitution was adopted, it does not follow that the power has no limitations." (p. 669)

This Court then continued its historical review by pointing out that by the act of 1867, as amended by the act of 1874,

> "the debtor for the first time was permitted either before or after an adjudication in bankruptcy, to propose terms of composition to his creditors to become binding *upon their acceptance by a designated majority* and confirmation by the judge." (p. 671; emphasis supplied).

Returning to the application of the bankruptcy statutes to railroads and specifically to Section 77, this Court said:

> "As outlined by that section [i. e. Section 77, as it *then* stood], a plan of reorganization, when confirmed, cannot be distinguished in principle from the composition with creditors authorized by the act of 1867, as amended by the act of 1874. * * * The constitutionality of the old provision for a composition is not open to doubt." (p. 672; part in brackets supplied).

This Court then turned to a discussion of the *Gebhard* case,* also cited by the petitioners. In the *Rock Island* case this Court quoted from its opinion in the *Gebhard* case as follows:

> "The confirmation and legalization of 'a scheme of arrangement' under such circumstances is no more than is done in bankruptcy when a 'composition' agreement with the bankrupt debtor, *if*

* *Canada Southern Railway Company v. Gebhard* (1883), 109 U. S. 527.

assented to by the required majority of creditors, is made binding on the non-assenting minority." (pp. 673-4; taken from 109 U. S. p. 536; emphasis supplied).

This Court concluded in the *Rock Island* case that

> "It follows, from what has now been said, that § 77, in its general scope and aim, is within the power conferred by the bankruptcy clause of the Constitution; and we so hold." (p. 675)

Thus, it was by analogy to "compositions" that Section 77 was found to be constitutional.

To the extent that Section 77, as amended, permits a court to confirm a plan *which has been accepted by a majority of the secured creditors of each class*—notwithstanding the fact that it has failed to receive a two-thirds vote of acceptance—it would seem that the same line of reasoning or analogy to bankruptcy compositions, which this Court followed in the *Rock Island* case, would sustain the *amended* statute.

The *North Western* case* is cited by the petitioners as "ending all constitutional doubt" on this subject. There was *dictum* in the District Court opinion in that case to the effect that a plan may be confirmed notwithstanding the size of the rejection vote but a careful examination of the case discloses that the statement was *dictum* only, that that question was not presented by the facts, was not argued to the Court and that the decision of that question was not necessary to a decision of the case. The fact was that a *majority* (50.37%) of the holders of the State

* *In re Chicago and North Western Railway Co.*, 7th C. C. A. 1942, 126 Fed. 2d 351, cert. denied (1943) 318 U. S. 793.

Line Bonds voting on the plan had voted to *accept* the plan. The question presented for decision was merely whether a plan could be confirmed which, although accepted by a majority vote of a class of creditors, had failed to receive the two-thirds vote mentioned in the statute. The opinion of the C. C. A. does not refer to the point specifically but a footnote to it quotes the following from the District Court opinion:

> "Furthermore, the power to confirm a composition over the objection of 33⅓% of the creditors is exactly the same kind of a power as the power to confirm a composition over the objection of 49.63%; * * *."

That much of the sentence quoted is not *dictum* and does not go beyond the facts and argument of the case there under consideration, but the District Court continued, with the following unsupported and uncalled-for *dictum:*

> "or for that matter over the objection of 100% of them. It is a bankruptcy power. * * *" (126 Fed. 2d 365-6, footnote 9, taken from June 25, 1941 unreported opinion of the District Court, *North Western* printed record Vol. 9, pp. 5428-9).

An examination of the briefs filed in the *North Western* case on behalf of Irving Trust Company, as trustee of the State Line Mortgage, and its opponents, indicates that no argument was made to the court relative to the effect of a majority *rejection*. That fact was not there present.

Recently, in the *New Haven* case,* the District Court has undertaken to confirm a plan notwithstand-

* *In re New York, New Haven & Hartford Railroad Co.* (D. C. D. Conn. 1945).

ing the fact that only 49.40% of the Old Colony bondholders voting accepted the plan. That decision has been appealed to the Circuit Court of Appeals for the Second Circuit and that appeal is now pending.

One fundamental limitation upon the bankruptcy power would seem obviously to be that no secured creditor may be compelled to surrender his security and to take something else in lieu of it unless the arrangement has at least been approved by a *majority* of the voting creditors of his class. Without that minimum safeguard, reorganization procedure would become reorganization by mere judicial (and Commission) fiat. . . .

This Court observed in the *Radford* case* that:

> "The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment." (p. 589).

The *Radford* case dealt with a question arising under the so-called Frazier-Lemke Act, which added to Section 75 of the Bankruptcy Act sub-section (s) relating to farmers who had failed to obtain the consents requisite to a composition under that Section. In holding the Frazier-Lemke Act unconstitutional, this Court observed:

> "Although each of our national bankruptcy acts followed a major or minor depression, none had, prior to the Frazier-Lemke amendment sought to compel the holder of a mortgage to surrender to the bankrupt either the possession of the mortgaged property or the title, so long as any part of

* *Louisville Joint Stock Land Bank v. Radford* (1935), 295 U. S. 555; 79 L. Ed. 1593.

the debt thereby secured remained unpaid." (pp. 581-2).

* * * *

"In no case of composition is a secured claim affected except when the holder is a member of a class; and then *only when the composition is desired by the requisite majority and is approved by the court.*" (pp. 585-6; emphasis supplied).

In discussing the power of the bankruptcy court to enforce a composition between creditors, this Court further observed:

"It is the same power, which a court of equity exercises when it compels dissenting creditors, in effect, to submit to a plan of reorganization approved by it as beneficial and assented to by the requisite *majority* of the creditors. *Shaw* v. *Railroad Co.*, 100 U. S. 605; *Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.*, 271 U. S. 445. Compare *National Surety Co.* v. *Corlett*, 289 U. S. 426; *First National Bank* v. *Flershem*, 290 U. S. 504" (p. 585; emphasis supplied).

As above stated, the Frazier-Lemke Act was held unconstitutional.

The August 27, 1935 amendments to Section 77 are discussed in a Columbia Law Review article "Amendment of the Railroad Reorganizaton Act" (1936—Henry J. Friendly), 36 Col. Law Rev. 27. After observing that the provision for confirmation of a plan notwithstanding its rejection "raises constitutional questions of the most serious character" (p. 32) and after referring to this Court's decision in the *Rock Island* case, previously discussed in this brief, the article points out that the *Rock Island* decision "was based specifically upon the analogy of a composition, which if assented to by the required

majority of the creditors, is made binding on a 'non-assenting minority'." (pp. 34-5). The law review article then goes on to say:

"*The history of composition and adjustment legislation both in England and in the United States reveals a consistent adherence to this principle of majority rule.* English composition statutes have always required the assent of *at least a majority* in number and amount of the creditors, and since 1869 they have required a majority in number and three-fourths in amount. In this country, the act of 1874, which introduced the principle of composition into our bankruptcy legislation, required the adherence of a majority in number and three-fourths in amount of the creditors present at the meeting and subsequent written confirmation by two-thirds in number and one-half in amount. The present Bankruptcy Act requires a majority in number and amount. The English Railway Companies Act of 1867, and the Joint Stock Companies Arrangement Act, the pioneer corporate reorganization statutes, demanded a vote of three-fourths in value of each class of security holders. With a single exception, the recent Federal legislation for the relief of debtors enacted prior to the present amendment has required either a two-thirds or a majority vote of a class affected by a plan and not otherwise protected.

"The fate of that exception, the Frazier-Lemke Act of June 28, 1934, *affords no ground for optimism as to the constitutionality of the provision under discussion*,—at least as applied to secured creditors. * * * *the Supreme Court's opinion holding the Frazier-Lemke Act unconstitutional reveals that there is serious question whether a secured creditor can be forced to accept even the*

fairest substitute for his security in the absence of assent by a majority of the class. * * *" (pp. 34-5; emphasis supplied).

Later on in the article, the following appears:

"* * * *the history as to compositions and schemes of adjustment is not to be lightly disregarded.* This history shows a general belief, both in England and in this country, that a creditor cannot fairly be deprived of his rights to have his security or his debtor's property applied to the satisfaction of his demands *except when enforcement of his will would obstruct a greater number of his class from achieving their reasonable desires.* The ultimate question is whether this belief is so deeply rooted in our thinking that its violation is a denial of due process of law. * * * *But it must be something more than an accident that, so far as has been discovered, no English or federal statute* (except the Frazier-Lemke Act) *has ever before authorized the court to interfere finally with a creditor's right to reach his security except when the judgment of the court and that of a majority of the class of creditors concurred.* Whether a plan is fair to a given class of security holders is a question not of law but of business judgment on which a court is peculiarly likely to err, and *it is sound policy to require the judgment of the court to be supplemented by the views of the persons whose investments are actually at stake.* Certainly the framers of the amendment were mistaken in thinking that because the court will not bind a minority when it believes the minority to be right, it follows as an irresistible conclusion that the court may constitutionally be empowered to bind a majority in cases where it believes the majority to be wrong." (p. 36; emphasis supplied).

CONCLUSION.

Under the admitted facts in the record, many of which are reviewed in the Statement, and for each of the several reasons set forth in the Argument, it is clear that the Circuit Court of Appeals was correct in its "conclusion that the Plan fails to meet the requirements of Section 77(e)" and "* * * that the General [Mortgage] Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, * * *". Accordingly, the Plan should be referred back to the Commission for further proceedings as provided in the statute and as directed by the Circuit Court of Appeals for the Tenth Circuit.

Respectfully submitted.

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Of Counsel.

February 15, 1946.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

Nos. 278, 279, 280, 281 and 282.

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, *et al.*,

Petitioners,

—against—

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *et al.*,

Respondents.

(and the other four cases numbered above).

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT.

APPENDIX TO BRIEF ON BEHALF OF RESPONDENT, CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE UNDER THE DEBTOR'S GENERAL MORTGAGE.

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THE COURT PRESS, N. Y. C.

APPENDIX TO BRIEF ON BEHALF OF RESPONDENT, CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE UNDER THE DEBTOR'S GENERAL MORTGAGE

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1. Abstract of Part of the Testimony of Witness, Miles C. Kennedy, at Confirmation Hearing, August 30, 1944 (R. 310-332)

My name is Miles C. Kennedy. I live at 45 Fifth Avenue, New York. I am a consulting engineer, a member of the firm of Coverdale & Colpitts, consulting engineers; office at 120 Wall Street, New York City.

"Q. Will you please give a brief statement of your professional experience?

The Court: Is there any question as to his qualifications by anyone?

Mr. Homire: We will waive any question as to that.

Mr. Gibson: We will do likewise.

The Court: All right.

Mr. Watts: Your Honor, may I inquire whether that goes to the extent of—I hope to bring out in these qualification questions the fact that the witness and his firm have in a very large number of railroad reorganizations served as special advisers and consultants to the bondholders, bondholder committees, creditor groups and the like.

The Court: That fact is well known to the Court and I presume it is to all the parties here.

Mr. Gibson: We so admit."

I have examined the two exhibits which have just been introduced, being City Bank Farmers Trust Company Exhibit 10 and Exhibit 11 [See R. 349, 350]. * * *

To the best of my knowledge, the substance of the information which is outlined in both of these tables, and particularly the table included in Exhibit No. 11 [See R. 350], has been available to the public and to the holders of the General Mortgage bonds. * * * The income accounts are, of course, published in the daily press, and all the information in regard to the plan has been in financial papers, dailies, weekly, statistical services and the manuals which are readily available.

In my opinion this is the kind of information which would and which should be carefully considered by the General Mortgage Bondholders in determining how they should vote on the acceptance or rejection of the plan of reorganization. I think it is very important information. * * *

I think one of the highly significant facts * * * is * * * that as of December 31, 1943, the last previous year end to the submission of the plan, all the interest on obligations senior to the General Mortgage Bonds had been earned with a margin of $3,859,306.00 to spare. In other words, if the amounts earned available for interest on the senior obligations had been paid to the holders of those obligations, the position of the General Mortgage would have been no worse than it was at the beginning of the receivership.

Now, as compared to that, the other significant fact is * * * that in the first plan filed, which was the debtor's plan, the General Mortgage was accorded 100 per cent treatment in new preferred stock. * * * That is, they would have gotten dollar for dollar in par amount in satisfaction of their claim as of that date, or their principal amount as of that date. The next plan was the Insurance Group plan of 1937 which gave the General Mortgage 100 per cent in new common stock. After hearings before an examiner of the Interstate Commerce Commission the examiner recommended fifty per cent in new common stock. The Interstate Commerce Commission in two subsequent plans awarded thirty-three and one-third per cent. One of these was in 1939, and one was in 1940. A certain discussion plan more or less agreed upon—I don't know exactly—in 1941 again gave the General Mortgage bonds fifty per cent. The Court's plan of 1941 brought the amount to 32.99 per cent, to practically thirty-three per cent, and in 1941, * * * the Insurance Group plan accorded the General Mortgage 47.42 per cent.

Then we get along to 1942 and the Interstate Commerce Commission cut the percentage down to five per cent, and in 1943 they doubled that treatment by giving them ten per cent. Now, coupled with that fact is that the earnings

of the property had been improving steadily since about 1937, when, * * * there was a deficit of $249,880.00 in income available for interest. *Those earnings increased very substantially*, due in part I should say to the generally increasing prosperity, *due in rather large part I should say to the improvements which were being made in the debtor's program, under which very large amounts were spent for improvements which it is reasonable to assume produced very substantial savings or increases in revenues.*

The figure $3,859,306.00, which I referred to, * * * represented the accumulated surplus up to December 31, 1943, of the income available for interest over the interest requirements of the so-called senior obligations. *It is true that the period during which that figure was built up included some abnormally good years, but it may also be said that some of these years were abnormally bad years*, and, furthermore, in some of these years in the period, perhaps all of them, the earnings were reduced because of the expenses incident to the very large improvement program which I just mentioned. * * *

I know in a general way what was done with the money which was earned but which was not paid out to the security holders. *Up to the end of 1943 the trustees under the direction of the Court had expended, I think about $37,000,000.00 in improvements, additions and betterments to the property.* All of that money did not come from the accumulated earnings set forth here. Part of it came from equipment trust issues I think in the amount of some five to six million dollars. Part of it was, of course, accrued in depreciation accounting, *but it is quite clear that the earnings of the property throughout this period in general have been used to improve and strengthen the property in the discretion and wisdom of the trustees and the Court.*

I am familiar with the fact that over the period as a whole there has been an increase in the cash and current assets over current liabilities. *There have been very substantial increases.*

I would start out with the assumption, I believe, that the trustees of this property were acting with all wisdom and discretion not only because they were appointed by this Court and confirmed by the Interstate Commerce Commission, but because I know and *I believe it is a matter of general information that the trustees have done an outstanding piece of work for this property.* I would therefore believe that in diverting funds from the payment of interest to investments in the property *the trustees were doing what they believed and what was for the benefit of the debtor's estate and for the security holders for whom they were trustees.* From that I draw the conclusion that they considered the investment of this money in additions and improvements much more beneficial to the security holders of the company than the payment to them of current interest, because *I do not believe that they would do anything to worsen the position of their security holders or any class of them;* certainly not willingly.

* * * * * * *

Now, of course, it is reasonable to believe that the expenditures that these trustees made have been productive and will be productive of very substantial earnings. I spent several years with the Pennsylvania Railroad making economic studies of the savings it had out of new work, the added traffic to be obtained by new lines and extension of lines, and I know very well an improvement that didn't earn fifteen per cent on its cost or was not estimated to earn fifteen per cent on its cost would receive no consideration whatever from the management, and *I therefore assume that these improvements or most of them could be expected to earn ten per cent to fifteen per cent or even more in some cases.*

Now, if that is the case the position of the bondholders is improved, and *even though money has in effect been borrowed from the bondholders through the non-payment of interest,* which has been used for making improvements, there is bound to be considerable income in excess of the

interest that will be paid on that money when interest is again resumed, and that benefit would flow down to the junior issues in the reorganization. *I should therefore conclude that the position of the General Mortgage—what I have already said is true—the position of the General Mortgage should be better rather than worse through the expenditure of this money by the trustees even though it has meant the piling of additional debt ahead of the mortgage.*

* * * * * *

I am not talking about maintenance. I am talking about improvements over and above the maintenance.

* * * * * *

You could have replaced various parts of the property in kind. Instead of that you went out and built better bridges than you had before. You bought better equipment than you had before. Understand I am not criticising in any way any part of this program. Relying upon the trustees, as I said, I have no inclination to criticise anything that was done. I am saying, however, that the money hat was used to make a substantial part of these improvements was in effect borrowed from the bondholders and claims piling up on the reorganization on which interest will be paid. * * *

I spoke before of a substantial improvement in the debtor's cash position as of December 31, 1943. If you will give me that 1943 report that Mr. Thompson introduced——

From page 12 of this Exhibit No. 8 [1943 Annual Report] which Mr. Thompson introduced this morning, the cash as of December 31, 1943, was $12,716,934.00. Temporary cash investments were $8,005,000.00. Total current assets were $33,915,000.00, roughly, and current liabilities were $23,517,000.00, also roughly, which gives net working capital of approximately $10,400,000.00.

In view of the cash distributions which have been and were being provided for security holders in numerous other reorganization proceedings before the Interstate Commerce

Commission and before the courts, it was in my opinion reasonable for the General Mortgage bondholders to assume that some of this cash to which I have just been referring might be used to reduce accrued interest on obligations prior to the General Mortgage bonds, and thus improve the position which the General Mortgage bondholders might expect in the plan of reorganization. I can think of several cases where cash distributions were made to reduce claims, and those cases, generally speaking received rather wide publicity, and it would be quite natural for bondholders not only in this company but in other companies to expect or have strong hopes that similar distributions would be made in these cases.

"Q. I come now, Mr. Kennedy, to the question for which I have been laying the groundwork by these previous questions, and first I want to read again certain language of subsection (e) of Section 77 of the Bankruptcy Act, which says that: 'if the plan has not been so accepted by the creditors and stockholders'—that means by the vote of two-thirds of each class of securities entitled to vote—'the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing,'—then I will skip a little—'that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts.' Without reading the balance of these requirements, *in your opinion, based upon your general experience in such matters and upon the testimony which you have just given, was the rejection of this plan by the General Mortgage bondholders reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts?*

"Mr. Gibson: Your Honor please, that forces an ultimate question of law. The statute implies whether your Honor is satisfied, not whether Mr. Kennedy is satisfied. We doubt if the witness is competent to express an opinion on that ultimately.

"The Court: I think the objection is good, but I will let him answer if you want it in the record.

"Mr. Watts: We are just asking his opinion.

"The Court: You are asking his opinion how someone else should make up their minds. He can answer, but I don't know what value it will have.

"A. *In my opinion it was.*"

* * * * * * *

On that day, November 1, 1935, there were $102,000,000.00 of obligations ahead of the General Mortgage bondholders. * * *

* * * * * *

The principal of the General Mortgage debt on November 1, 1935, was in the neighborhood of twenty-nine million. So, * * * there was one hundred thirty million of debts to be compared with the one hundred and forty million capitalization. By that I mean principal amount. *So that if this plan of reorganization had been put into effect on November 1, 1935, on the basis of any valuation that has been used in this proceeding, I should judge that the General Mortgage claim would have received at least 100 per cent in new securities or shares under that capitalization.*

Now we are nine years or thereabouts later. The indebtedness they are putting ahead of the General Mortgage bonds now in this plan of reorganization which is now before the Court (referring to documents) I should say is about $140,000,000.00. That is Rio Grande securities alone, not the Denver & Salt Lake. * * * So that through lapse of time they have allowed to be accumulated on creditor's claims ahead of the General Mortgage bonds and other creditors some thirty-odd million dollars.

*And that has reduced the distributive share of the General Mortgage Bonds in the securities of this reorganization unless the capitalization is increased to allow for the improvements they have made, * * * during this receivership period, which have added to the value of the property, and certainly have added very substantially to its earning power.*

But they have not increased the capitalization over and above the original capitalization by more than $7,000,000.00. And the result is that the General Mortgage Bonds are shoved down below thirty million more than would have been the case on November 1, 1935. * * * That has been the effect. * * * *During this time this property has been improved very substantially.*

The figures of the improvement program, what has been invested, there has been approximately thirty-seven million, as I recall, invested from the date of receivership to the date of December 1, 1943.

We have before us for every year a statement of net income which I have seen. For every year of the operation of these trustees, and before reaching that figure of net income, all maintenance expenses are deducted from income. * * * *I think very definitely in this period of improvement of this property there has been an actual improvement in the useful value of this property, in the utility of this property.* To form any other conclusion you would have to conclude that the trustees had not known their business, didn't know what they were doing.

I know that lines have been abandoned during that period. I wouldn't have to look at it, Mr. Hodges, to give an opinion as to whether the abandonment of these lines has improved the general efficiency and utility of the plant. I know *perfectly well that the Interstate Commerce Commission approves the abandonment of a line which means that line has been a decided drain on the system, and therefore the abandonment has meant an improvement to the property.*

2. Abstract of Part of the Testimony of Witness, Ralph E. Morton, at Confirmation Hearing, August 30, 1944 (R. 335-339)

My name and address is R. E. Morton, 22 William Street, New York City. I am one of two vice-presidents in charge of the Corporate Trust and Reorganization Department of the City Bank Farmers Trust Company, having been assigned to that department in May, 1927. I have as part of my personal work in that department the administration of trusts created by railroad mortgages. City Bank Farmers Trust Company has had many railroad mortgage trusteeships. At the present time I am administering approximately seventy-five railroad issues in my division of the department. The trust company, either under its present name or its former name of The Farmers' Loan and Trust Company, has taken part in many railroad reorganizations. In the course of the work I personally have done in connection with the reorganization of corporations which have given mortgages to the trust company, I have been consulted frequently by the holders of the securities with respect to the merits of plans of reorganization or readjustment which have been from time to time proposed for the securities, in a great many cases.

* * * * * *

In the last ten years I have been working on the railroad reorganizations of the Chicago, Milwaukee, St. Paul & Pacific, the Chicago & North Western, the Erie, the New York, New Haven & Hartford, the Minneapolis & St. Louis, the Savannah and Atlanta, the Missouri Pacific, and I think that covers a fair part of the list.

* * * * * *

I am familiar with the exhibit which was introduced this morning as City Bank Farmers Trust Company Exhibit 10 [See R. 349] which is a table of income available for interest

and interest upon certain senior securities. I am also familiar with the table which was introduced as City Bank Farmers Trust Company Exhibit 11 [See R. 350] which refers to some eleven reorganization proposals which have been made in this case as well as the provision made for the claims of the General Mortgage Bonds in those proposals, and set alongside of them certain figures in regard to the current earnings of the debtor available for interest in the years in which the proposal was made, as well as the net situation up to the last previous December 31st prior to the date on which such proposal was made with respect to such earnings available for interest as contrasted with such senior interest requirements.

I have been from time to time, as the various figures were available, in a general way familiar with all the figures which are for convenience set forth in tabular form on those exhibits.

I have considered the relationship between the several treatments proposed for the General Mortgage Bondholders from time to time as contrasted with what appeared to be the current earning situation of the debtor at the time those proposals were made. I have been following the earnings monthly, Mr. Watts.

From my communications from bondholders, whether in the form of personal visitations, telephone conversations or letters, I am certain that at least some of the bondholders have considered the proposals made for the General Mortgage Bonds in the light of those figures.

"Q. In your opinion does the current earning situation of a railroad generally have any bearing upon the reasonableness of a proposal to the creditors of that railroad, particularly where it is a proposal that such creditors should accept in a plan for reorganization securities different from what they hold? A. Well, in my opinion the earnings have some bearing.

"Q. And does the result of operations to the last practicable date have a bearing upon the reasonableness of the proposal made? A. Yes, I think so.

"Q. Did you, Mr. Morton, or anyone else in the Corporate Trust Department of the City Bank Farmers Trust Company make any recommendation to any holder of General Mortgage Bonds as to how they should vote on this plan of reorganization? A. *The City Bank Farmers Trust Company as Trustee under this General Mortgage made no recommendation to any bondholder as to whether he should vote to affirm or reject the plan.*

"Q. Can you state briefly why you followed that policy? A. Well, we had been making recommendations before the Commission and Court over a period of years on behalf of bondholders. We had been approached I suppose a half dozen times by various groups of bondholders who were giving consideration to the formation of a protective committee for the bonds. We have offered them all encouragement in each case to go ahead with the formation of the committee. After the plan was approved by the Court we thought that it was only appropriate to let the bondholders decide on the basis of their individual circumstances as to whether or not they wished to accept or reject the plan.

"Q. So the vote of 79.33 per cent of the General Mortgage Bondholders who voted to reject the plan was not based in any way upon any recommendation by the Mortgage Trustee that they should vote against the plan? A. It was not."

. . . . . .

"Q. *Mr. Morton, on the basis of the facts which for convenience are arranged in tabular form on these two exhibits, and on the basis of all the information that was available to the bondholders from time to time, was it in your opinion reasonable or unreasonable for the bondholders to vote to reject the plan?* A. *Yes, reasonable.*

"Mr. Gibson: Your Honor please, an objection to the preceding question of the preceding witness was sustained.

"Mr. Watts: No, it was not sustained.

"Mr. Gibson: I object on the ground that the question is calling for an opinion on an issue for the Court to decide.

"The Court: Objection sustained."

3. Report of Federal Coordinator of Transportation on Transportation Legislation (part of H. Doc. No. 89, 74th Congress, 1st Session)*

January 21, 1935

To the Interstate Commerce Commission:

In accordance with the duty laid upon the Federal Coordinator of Transportation in section 13 of title I of the Emergency Railroad Transportation Act, 1933, the purpose of this report is to submit recommendations for further legislation to improve transportation conditions throughout the country, which the Commission shall transmit with its comments to the President and to the Congress (p. 1).

* * * * *

Bankruptcy Act Revision

* * * * *

Section 77 was designed with the purpose of expediting reorganizations, but there has been slow progress under it. No better progress has been made in the equity proceedings. The depression has been largely responsible for this slowness, but there are deficiencies in section 77 which should be cured by amendment, and particularly by amendments designed to minimize the difficulties in obtaining the assents of creditors and shareholders.

Among the important amendments proposed are these:

1. While it is undesirable to amend section 77 in a manner to force reorganizations where the times are not propitious for sound reorganizations, it is clear that the

* The full Report, of which this is an extract, was sent to the President, the President of the Senate, and the Speaker of the House of Representatives with a Letter of Transmittal, dated January 23, 1935, by Hugh M. Tate, as chairman of the Interstate Commerce Commission.

law should be so arranged as to require reorganizations as soon as conditions are right and to prevent obstructive action by minorities for purposes of selfish gain. The present act was a right step in this direction in providing that approval of a plan by two-thirds of any class of creditors or shareholders is binding upon the minority of such class. But a fair and equitable plan may be defeated if not approved by two-thirds. As the law is now drawn, it seems to be generally believed that the power lies in minorities to block any reorganization. While it is not thought desirable to dispense with the securing of consents from the creditors and shareholders, it is clear that there should be provisions whereby a court may, under some circumstances, make effective a fair and equitable plan over the dissent of minorities, under an arrangement insuring a full hearing to all of the parties concerned and an adjudication by the Commission and the court establishing the fairness of the plan. It is, therefore, proposed to liberalize the procedure so that the Commission, considering the plans of any who may propose them, shall tentatively approve a plan which shall be passed upon by the court after hearing the objections of any party of interest. The plan, if approved by the court, shall then be submitted to the interested creditors and shareholders. The consents of two-thirds of each class of creditors and stockholders shall bind the minorities in such classes. But, if the court shall find that the plan is fair and equitable, it may make it effective, even if not so approved.

Arbitrary compulsion of plans over the dissents of the interested classes is not intended, nor is it believed that the courts will override strong dissents by any large number of such classes, or by a single large class, excepting where it is established that they have no interest in the property. Rather, the purpose is to prevent the obstruction of plans which are favored by the larger classes of creditors or shareholders, but which are obstructed by minorities in the smaller classes in the attempt to secure unduly preferential treatment. From a legal standpoint

there are no apparent objections to this course. It puts emphasis upon the adjudication of these rights by providing for hearings before the Commission and the courts under prescribed principles of substantive law, whereby there must be, among other things, a proper recognition of the priorities of the respective interests (pp. 161-2).

* * * * *

The bill providing for the proposed revision of section 77 of the Bankruptcy Act is herewith submitted as Appendix X (p. 103). * * *

JOSEPH B. EASTMAN,
Federal Coordinator of Transportation

(p. 105)

4. Extract from Report No. 1283, dated June 21, 1935, House of Representatives, 74th Congress, 1st Session

HOUSE OF REPRESENTATIVES

74th Congress, 1st Session } Report No. 1283

REORGANIZATION OF RAILROADS UNDER THE BANKRUPTCY ACT

June 21, 1935.—Referred to the House Calendar and ordered to be printed

Mr. Sumners of Texas, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany H. R. 8587]

The Committee on the Judiciary, to whom was referred the bill, H. R. 8587, to amend section 77 of the Bankruptcy Act, after consideration, report the same favorably to the House with the recommendation that the bill do pass.

The purpose of the bill is to provide amendments which have been demonstrated as necessary by experience in the administration of section 77 of the Bankruptcy Act, entitled "Reorganization of Railroads engaged in Interstate Commerce", which was enacted by the Seventy-second Congress, second session, (act of Mar. 3, 1933, 47 Stat. 1477; U. S. C., title 11, sec. 205). About 55 railroads with a mileage of something over 43,000 miles are now involved in bankruptcy or receivership proceedings. Hon. Joseph B. Eastman, the Federal Coordinator of Transportation, in a report to Congress (transmitted Jan. 23, 1935; 74th

Cong., 1st sess., H. Doc. No. 89)* recommended the revision of section 77 and submitted a bill incorporating his proposed amendments (pp. 35, 100, 229). That bill has been the basis of the work of your committee (p. 1).

* * * * *

One of the main difficulties with reference to the present act is that a minority of more than one-third of any one class of creditors can obstruct and prevent the approval of any plan. This bill provides that two-thirds of those of each class who vote upon the plan will bind the dissenters and those of the class who fail to record their votes as provided by the act. It also provides that the court may make effective a fair and equitable plan over the dissent of such minorities. Under its provisions, the Commission will tentatively approve the reorganization plan; it will then be passed upon by the court after hearing the objections of all parties in interest. Before approving it, the court must find that the plan is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders.

The plan, if approved by the court, will then be submitted to the creditors and shareholders. The consent of two-thirds of those of each class who vote upon the plan will bind the remainder in that class. But the judge may make the plan effective, even if not so accepted, if he finds that it conforms to the requirements just stated, provides fair and equitable treatment for the interests of those rejecting it, and that their rejection is not reasonably justified in the light of their respective rights and interests (pp. 2-3).

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* Extract from H. Doc. No. 89 appears in this appendix at pages 1-3.

In order to protect the rights of stockholders and creditors which might be injured by a reorganization on the basis of depressed conditions in the event of an early return to prosperous times, paragraph (b) clause (3) provides that the plan may require the issuance of securities in the form of options or warrants to receive, or to subscribe for, the securities of the reorganized company to security holders who otherwise are not provided for in the plan (p. 3).

5. Extract from Report No. 1336, dated July 29, 1935, Senate, 74th Congress, 1st Session

SENATE

CALENDAR No. 1388

74th Congress, 1st Session } Report No. 1336

REORGANIZATION OF RAILROADS UNDER THE BANKRUPTCY ACT

July 29 (calendar day, August 16), 1935—Order to be printed

MR. WHEELER, from the Committee on Interstate Commerce, submitted the following

REPORT

[To accompany S. 1634]

The Committee on Interstate Commerce, to whom was referred the bill (S. 1634) to amend section 77 of the Bankruptcy Act, having considered the same and adopted certain amendments, report the bill back favorably to the Senate with the recommendation that it be passed. A similar bill was introduced in the House of Representatives and was reported favorably by the Committee on the Judiciary of the House with certain amendments (H. R. 8587; Rept. 1283, June 21, 1935). The bill, S. 1634, as amended, which your committee hereby recommends, is the same as the bill, H. R. 8587, as reported by the Committee on the Judiciary of the House in the said report. H. R. 8587 as thus reported was passed by the House of Representatives, with certain amendments made on the floor, on August 15, 1935. * * * (p. 1).

The purpose of the bill is to provide amendments which have been demonstrated as necessary by experience in the administration of section 77 of the Bankruptcy Act, entitled "Reorganization of Railroads Engaged in Interstate Commerce", which was enacted by the Seventy-second Congress, second session (act of Mar. 3, 1933, 47 Stat. 1477, U. S. C., title 11, sec. 205). It is necessary that this bill be passed now because 85 railroads, with a mileage of something over 58,815 miles, are now involved in bankruptcy or receivership proceedings and, for reasons to be here stated, amendments of the law are essential to enable the efficient reorganization of these properties (p. 1).

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Hon. Joseph B. Eastman, the Federal Coordinator of Transportation, in a report to Congress (transmitted Jan. 23, 1935; 74th Cong., 1st sess., H. Doc. No. 89)* recommended the revision of section 77 and submitted a bill incorporating his proposed amendments (pp. 35, 100, 229). That bill has been the basis of S. 1634 and H. R. 8587.

* * *

The important amendments to section 77 incorporated in S. 1634, as amended, are as follows:

(1) While section 77 is in general an admirable piece of legislation, in certain respects it has been found unworkable. The act was designed to prevent the obstruction of reorganizations by minorities by providing that the approval of a reorganization plan by two-thirds of any class of creditors or security holders is binding upon the minority in a class. But, if not so approved, a fair and equitable plan may be defeated. Not only may one-third of the security holders of any class prevent a fair plan from binding that class and thus require that their securities be bargained for, but the mere failure to vote upon a plan by those holding one-third of the securities of a single class

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* Extract from H. Doc. No. 89 appears in this appendix at pages 1-3.

will effectively block any reorganization. The formidability of such obstructive possibilities appears clearly in the pending reorganization of the Missouri Pacific, where the claim is made that there are 72 different classes of security holders. One bank loan from J. P. Morgan & Co. is put in a separate class. Each of such classes of creditors, if it does not agree to a plan, can drive a bargain with those endeavoring to reorganize the company, and is in a superior bargaining position. Further, the consent of two-thirds of each class of stockholders must be acquired, unless, by an elaborate valuation proceeding, it is proved that the value of the property is so low that the stock has no interest. This is an effective obstruction. Such valuation proceedings, if the appraisal method is followed, are of a volume almost unparelleled in any other sort of litigation. In a pending reorganization, the Commission has postponed such action in the hope that the act will be amended.

In order to remedy these defects, S. 1634, as amended, provides that two-thirds of those of each class who vote upon a plan will bind the dissenters or those failing to vote. But it also provides that the court may make effective a fair plan where the parties do not agree. If the Commission tentatively approves a reorganization plan, it is submitted to the court for approval. The court must find that the plan is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders. These standards require that the plan be prepared with scrupulous regard for the rights of all the parties. The plan, if thus approved by the court, will then be submitted to the creditors and shareholders. If two-thirds of each class consent, the plan will bind the remainder of each class. But the judge may make the plan effective, even if not so accepted, if he finds that it conforms to the requirements just stated, provides fair and equitable treatment for the interests of those re-

jecting it, and that their rejection is not reasonably justified in the light of the respective rights and interests. These provisions give complete due process of law from a procedural standpoint, there being provision for full hearings both before the commission and the court. Within the broad powers of Congress under the bankruptcy clause as recently declared by the Supreme Court in *Continental Illinois Bank & Trust Co. v. Chicago, Rock Island & Pacific Ry. Co.* (55 Sup. Ct. Rep. 595), the provisions also afford due process of law in fully protecting the property rights which are involved (pp. 2-3).

(2) S. 1634, as amended, is designed to protect the stockholders and creditors against unnecessary sacrifice in reorganizations made in a period of depression, when conditions are transient. In order to protect the rights of stockholders and creditors who might be injured by a reorganization on the basis of depressed conditions in the event of an early return to prosperous times, paragraph (b) clause (3) requires that the plan may allow the issuance of securities in the form of options or warrants to receive, or subscribe for, the securities of the reorganized company, to security holders who are not otherwise provided for in the plan (pp. 3-4):

6. Extract from Congressional Record, Vol, 79, Part 12, pages 13298-301, containing statements and debate in the House of Representatives, 74th Congress, 1st Session, on August 15, 1935 in connection with the proposed amendment of the Bankruptcy Act (H. R. 8587).

Mr. SUMNERS* of Texas. Mr. Chairman, this bill has to do with railroad reorganization * * * (p. 13298).

The Congress adopted legislation known as "section 77" of the Bankruptcy Act. The general plan of this legislation was to have the persons in interest agree upon a plan of reorganization. I shall not go into the details, but one difficulty that has been encountered, which, according to persons in best positions to know, makes it impossible to reorganize, is that the persons in interest group themselves into a great many classes. I believe in the Missouri Pacific case there were probably 72 classes. Under the law as it is now, reorganization cannot be effected unless the consent of two-thirds of each class is obtained.

This legislation, of course, we all know is largely experimental. I would not undertake, on my responsibility, to tell you I feel certain that the bill that is offered will work. We do not know. However, those in the best position to know feel hopeful that the bill that is offered will work. It seeks to get around the difficulty of permitting one class to block a plan. We pursue a method very similar to the present method of getting a plan presented. * * * (pp. 13298-9).

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To preserve rights of stockholders and creditors, not otherwise provided for, which might be injured by reorganization under depressed conditions, a "rain check" provision for the issuance of options or warrants to receive securities in the reorganized company in the event of early

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* Mr. Summers was in charge of the bill in the House of Representatives.

return to prosperous conditions may be included in the plan.

Two-thirds of the creditors of each class who vote will bind the class instead of the two-thirds of the entire class required by present law.

In the event the consent of two-thirds of those who vote is not obtained, the judge may nevertheless effectuate the plan if he finds that the objections are not reasonably justified in the light of the respective interests of the objectors (p. 13299).

* * * *

Mr. McFARLANE. What changes in the present law does this bill make, briefly stated?

Mr. SUMNERS of Texas. The most important change is that whereas under the present law there is required the consent of two-thirds of each class, it is made possible for the Commission and the court, after consideration of the plan—and they may modify the plan—if it is a fair and just plan and meets the constitutional requirements, it is possible to have a plan effectuated which has not been approved by two-thirds of each class (p. 13299).

* * * *

Mr. BIERMANN. It now takes two-thirds, and under your plan it states no definite number?

Mr. SUMNERS of Texas. That is right; and we feel that we have fully protected the constitutionality of the bill by providing that the plan must meet with—I have not the exact language of the bill in my mind—but it must comply with the law of the land (p. 13299).

* * * *

Mr. MICHENER. * * * In passing upon this bill we are not embarking upon a new policy. When the Congress passed section 77 of the bankruptcy law this method of railroad reorganization was given legislative sanction. The

purpose of this legislation is to accelerate railroad reorganization as contemplated when section 77 was enacted.

Before the enactment of said section 77 the only method by which a railroad might be reorganized was through the equity courts. The costs were unconscionable. The delays were interminable. And, 9 times out of 10 an agreement between the executives and the primary security holders resulted in the wiping out of the small equity holders. * * * (p. 13300).

* * * * *

The genesis of this bill was in the office of the Coordinator of Railroads. Mr. Craven, counsel to the Coordinator, presented a bill to our committee. It has been rewritten many times. Mr. Craven has given splendid assistance. He cooperated at all times and never dictated. He apparently had no pride of authorship but his was a spirit of helpfulness. Many crude committee amendments have been worked out by Mr. Craven, and I am sure that I speak the sentiment of the entire committee when I utter this word of appreciation (p. 13300).

* * * * *

Personally, I do not believe that this is the opportune time to force unreasonable reorganization of the railroads. Due consideration must be given under these amendments to the equities and priorities of those interested. And that which is an innovation provides them with what we in the committee came to call the "rain check" provision of the bill. This provision will be explained by the gentleman from Nebraska [Mr. McLaughlin]. It guarantees to the last equity holder every possible chance to realize on his investment if business does pick up and the railroads again become profitable (p. 13300).

* * * * *

Mr. McLaughlin. Mr. Chairman, the bill under consideration has had the attention of the Committee on the

judiciary and of a special subcommittee of that committee since this Congress began its present session, as has been outlined by my colleague from Michigan [Mr. MICHENER]. In the drafting of this bill the committee has had the able assistance of Mr. Craven, attorney for the Coordinator of Transportation, Mr. Eastman, but he has not dictated this bill in any sense, and has been entirely cooperative in the matter of amendments or changes to the bill as it was originally suggested by him (p. 13301).

I call your attention to the outstanding features of this bill with relation to the features of the present law which need correction. The present act provides that two-thirds of those voting, whether they be creditors or stockholders, can bind all of a class, instead of two-thirds of the entire class, as in the present law. In other words, under the present law, a minority of one-third may block a reorganization. That is corrected by the bill H. R. 8587 which is now before us.

Second, the act provides that the court may make the plan operative over dissenting creditors, if he finds that their rejection is not justified in the light of their interest. This provision facilitates reorganizations in those cases where no reasonable objection is presented (p. 13301).

One of the important features of this bill is what is known in the parlance of the committee, as the "rain-check feature", which provides that stockholders may receive evidences of their interest of participation in the corporation, so that if the rehabilitation of the railroad reaches a point where the stock again has a value, the stockholders automatically participate as they did under the old corporation (p. 13301).

7. Extract from Congressional Record, Vol. 79, Part 13, pages 13764-8 containing statements and debate in the Senate, 74th Congress, 1st Session, on August 20, 1935 in connection with the proposed amendment of the Bankruptcy Act (H. R. 8587).

Mr. WHEELER.* Mr. President, I wish to make a brief explanation of the bill and the reason for the amendment of section 77 of the bankruptcy act (p. 13764).

* * * * *

D. H. R. 8587 is the result of a general overhauling of the act and includes the following important amendments:

First. The most important changes are provisions permitting making present plans effective. Under the present law, if more than one-third dissent or fail to vote, a plan, which is fair and equitable is blocked—the act requiring that two-thirds of each class must approve the plan. There are said to be 72 classes of creditors and stockholders in the Missouri Pacific case and 35 of 40 classes in the Rock Island case. In the instance of the Missouri Pacific, J. P. Morgan Co. has a bank loan of $6,000,000—I am merely citing this case as an illustration—classified in a single class, and has in hock the controlling stock interests of the Van Sweringens. This means that it is impossible to get through a plan without either meeting the Morgan's terms or paying the value of their interest in cash.

In other words, it makes it possible for a man who holds something over one-third of some one small class of debt absolutely to say that no reorganization plan can take place no matter how fair it may be, "Unless you either buy me out or pay me the full amount of my debt to the detriment of the other classes" (p. 13764).

* * * * *

* Mr. Wheeler was in charge of the bill in the Senate.

Mr. Wheeler. * * * It is not possible under the present law to overcome the obstruction of the equity holders without a valuation which will establish that they have no equity in the property. The valuation hearings are almost without any equal in jurisprudence for size and expense. Consequently, in the pending Frisco reorganization, the Commission has found it necessary to postpone any further action until the act is amended; otherwise they would have to go through a complete valuation of the Frisco system, and it would take years for them to complete that valuation in order to get a reorganization as the set-up is at present.

These difficulties are overcome by the amendments which are proposed as follows:

The bill provides that if two-thirds of each class approve the plan it will bind the minorities.

It also provides that the court may make effective a plan where two-thirds do not agree, provided the court finds that the plan is fair and equitable, affords due recognition of the rights of each class of creditors and stockholders, will conform to the requirements of the law of the land, and that the rejection of the plan is not justified in the light of the respective rights of those rejecting.

Mr. Hastings. Mr. President, will the Senator yield?

Mr. Wheeler. I yield.

Mr. Hastings. The old bill provided that two-thirds of any class should be controlling, but this bill provides that two-thirds of those voting shall control; is that not correct?

Mr. Wheeler. Yes; that is, of each class.

Mr. Hastings. That is correct.

Mr. Wheeler. In the Van Sweringen case there are said to be 72 different classes.

Mr. Hastings. Mr. President, I am not complaining about it, but I desired to point out to the Senator, as the Senator went along, that there has been a change now, so instead of being two-thirds of the class, it is two-thirds of the voting in the class.

Mr. Wheeler. That is correct (p. 13764).

* * * *

Third. It is intended to protect the stockholders and creditors against injustice due to reorganizations based on depressed conditions which may be transient. Paragraph (b), clause 3, page 6, line 11, authorizes the issuance of options or warrants to receive, or subscribe for, securities—these being so-called "rain check" securities.

In a recent reorganization of an industrial concern many of the stockholders were completely wiped out. They were given no new stock. They received nothing at all.

Then after reorganization business began to pick up because of more prosperous conditions, but these stockholders who had invested their money remained completely wiped out, while other investors reaped the reward. This so-called "rain check" device is to protect that class of stockholders (p. 13765).

* * * * * * *

Mr. WHEELER. * * *

Coming now to the question of due process:

Before the reorganization can take place the court must make the following findings:

> That the plan is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders. These standards require that the plan be prepared with scrupulous regard for the rights of all the parties. The plan, if thus approved by the court, will then be submitted to the creditors and shareholders. If two-thirds of each class consent, the plan will bind the remainder of each class. But the judge may make the plan effective, even if not so accepted, if he finds that it conforms to the requirements just stated, provides fair and equitable treatment for the interests of those rejecting it, and that their rejection is not reasonably justified in the light of the respective rights and interests. These provisions give complete due

process of law from a procedural standpoint, there being provision for full hearings both before the commission and the court. Within the broad powers of Congress under the bankruptcy clause as recently declared by the Supreme Court in *Continental Illinois Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Ry. Co.* (55 Sup. Ct. Rept. 595), the provisions also afford due process of law in fully protecting the property rights which are involved (pp. 13765-6).

* * * * * * *

Mr. HASTINGS. * * *

With respect to the particular section, my understanding is that Mr. Craven, counsel for the Coordinator, who has been working diligently for at least a year upon the subject, found, as the railroads have found, many difficulties. For instance, I doubt whether anyone knew little or nothing about it would suspect that there could be 72 classes of creditors of any great railroad corporation in the country. It is realized, of course, how difficult it is to get 66⅔ percent of the creditors of 72 classes to agree.

Originally the question was—and, of course, it was to be decided by the Congress itself—whether or not one-third of the creditors should be compelled to agree with the opinion of two-thirds. Anyone who has had anything to do with the matter of reorganizing a corporation has had the experience of having some man or some few people standing out, demanding 100 percent payment of their claims, and thereby preventing reorganization of the corporation. It was sought to get away from that difficulty.

I do not recall that the Senator from Montana [Mr. Wheeler] emphasized this point, but I wish to emphasize it and express my own opinion with respect to the change proposed to be made in the law. The original law provided that 66⅔ percent of all classes must agree to the plan of reorganization; and if they should not agree, the court would have the right to ascertain the value of their claims and to pay them in cash. The bill changes that in two particulars, and this is of great importance.

In the first place, the bill provides that 66⅔ percent of those voting shall decide the question. That, I believe, is not unreasonable. It must be realized that in railroad corporations, with the securities scattered all over the country, it is frequently very difficult, even if the security holders agree, to get in touch with them and to get 66⅔ percent of a particular class. I think it is not unreasonable to provide that 66⅔ percent of the class which is represented shall vote and shall determine whether that class shall agree with the plan or whether it shall not.

There is a matter in the bill which is of greater importance. Even if no vote at all is obtained from a certain class, even if the whole class objects, it is provided that the court, if it finds the plan to be equitable and fair for that particular class, may force that class to agree even though all in that class object. The court, of course, will go a long way before agreeing to that if there be a real controversy. Of course, if the court should find some particular class refusing to participate simply for the purpose of holding up the reorganization, it could deal with the situation under the amendment proposed in the bill (p. 13766).

* * * * *

Mr. KING. Suppose the 1 class out of the 20 or 30 or even 70 held a preponderating interest in the corporation, either in the stock or the bonds or as a creditor, and the corporation or the person holding the preponderating interest objected, could it or he be forced to accept the terms?

Mr. HASTINGS. They could be under this plan, always with the approval of the court and with the right of appeal if the court dealt unfairly with them (p. 13766).

* * * * *

Mr. WHEELER. Not only must it be approved by the court, but it must be approved also by the Interstate Commerce Commission.

Mr. HASTINGS. Yes; I had overlooked that fact.

Mr. WHEELER. There is a double check upon the situation under that provision.

Mr. HASTINGS. Yes; there is a right of appeal to the circuit court from the decision of either of them.

Mr. WHEELER. Yes. As the Senator from Delaware pointed out, if we have as many as 72 classe of creditors, one class may come in and say to all the rest, "Unless you pay us out in cash we will hold up any reorganization." Everybody appreciates that the bill which the Senator from Delaware introduced originally was a step in the right direction. As he said, it was passed hurriedly toward the end of the session for the purpose of permitting reorganization, but it was found it did not work out practically.

Mr. HASTINGS. I may say to the Senator from Utah [Mr. King] that Congress is undoubtedly giving to the courts and to the Interstate Commerce Commission very great power. There is no doubt about that. However, so far as I am concerned, I have always been willing to leave such questions as are here involved to the Federal courts of the land, which, I think, constitute the finest branch of our Government, with the right of appeal. Occasionally the courts will make a mistake and occasionally an injustice will be done, but some place we have to leave that authority.

In this particular instance there is a double check. It is necessary to have the approval of the Interstate Commerce Commision and the approval of the district judge before whom the matter is being tried, and then there is always the right of appeal to the circuit court. Although we are giving this very great authority, I am quite satisfied that it has become necessary in order to make the bill workable that we should give that unusual authority (pp. 13766-7).

* * * *

Mr. KING. Suppose a majority of the bondholders—and I suppose there would be a mortgage or trust deed to secure the payment of the bonds—should determine to go

into court and foreclose for the purpose of obtaining judgment relief for the creditors. Under the bill they would be denied that opportunity, would they not (p. 13767)?

* * * *

Mr. WHEELER. The bill provides just the same as the ordinary statute for composition of the debts of the railroad company (p. 13767).

* * * *

Mr. KING.

The Bankruptcy Act, of which the measure before us is supplemental, was designed to aid the crippled railroads and to bring about, if possible, reorganizations so that they might render improved service to the public and prevent the stockholders and the owners and holders of securities from sustaining irreparable losses (p. 13768).

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

Nos. 278-282

RECONSTRUCTION FINANCE CORPORATION and others,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY and others,

Respondents.

BRIEF OF THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY

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February 15, 1946.

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BRIEF OF THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY*

Statement

This proceeding comes to this Court on writs of *certiorari* to review an Order or Decree of the United States Circuit Court of Appeals in the Tenth Circuit, dated May 10, 1945, which reversed two separate Orders of the District Court for the District of Colorado (Judge SYMES)—one an Order dated October 25, 1943, approving a Plan of Reorganization for the Respondent, The Denver and Rio Grande Western Railroad Company (herein called the Debtor) under Section 77 of the National Bankruptcy Act†

* The Respondent, The Denver and Salt Lake Western Railroad Company, a wholly owned subsidiary of The Denver and Rio Grande Western Railroad Company, concurs in and adopts this Brief.

† 11 U. S. C. § 205.

(herein referred to as Section 77); the other an Order dated November 29, 1944 confirming the same Plan of Reorganization after its rejection by the requisite percentage of the Debtor's General Mortgage Bonds (Tr., fol. 269).

The Debtor opposed the granting of the Petition for these writs of *certiorari* but believing that if this Court should determine to issue the writs it might desire a broad base for a reconsideration of its decisions rendered March 15, 1943, in the *Western Pacific* and the *Milwaukee* cases* the Debtor itself filed a separate Petition for a writ of *certiorari* which was designed to afford such a base should this Court desire it (No. 286, Oct. Term, 1945).

Questions Presented

The Question: What are the Questions Presented is one that may prove controversial. We feel that this question is not clarified by the Petition and Briefs of the Petitioners and that vital issues have been obscured.

As noted above there were two appeals from the District Court to the Circuit Court of Appeals. The appeals were argued separately and at different times—the appeal from the Order *approving* the Plan of Reorganization taken only by the Debtor was argued at Wichita, Kansas, on November 13, 1944; the appeal from the Order *confirming* the Plan taken by the Debtor and also by the Trustee of the General Mortgage and the Trustee of the Missouri Pacific Railroad Company was argued at Denver, Colorado, on March 14, 1945 (Tr., fols. 746; 784).

There can be no doubt at all under the language of sub-section (e) of Section 77 that the appeal from the last mentioned Order presented every question that was pre-

* *Ecker, et al. v. Western Pacific Railroad Corporation*, 318 U. S. 448; *Group of Institutional Investors, et al. v. Chicago, Milwaukee, St. Paul and Pacific Railroad Company*, 318 U. S. 523.

sented to the Court at Wichita plus a number of new and additional questions.

Sub-section (e) provides for the filing of Objections to a Plan of Reorganization certified to the District Court; a hearing upon such Objections and *after* such hearing if Objections have been filed but without a hearing if Objections have not been filed, an approval of the Plan if the Court finds that it meets all of the requirements specified in Clauses (1) to (3) of the first paragraph of said sub-section which include a finding that the Plan "is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders and will conform to the requirements of the law of the land regarding participation of the various classes of creditors and stockholders." If the Court finds that all of these requirements have been met an Order of Approval is granted as of course, subject to the general power reserved to the Bankruptcy Court as a court of equity and also implicit in sub-section (g) to do justice at any stage of the proceeding. But approval is not confirmation. *There must be further and very vital judicial action.* Sub-section (e) to this end provides that after the Plan has been approved by the Court it shall be submitted for acceptance or rejection by participating creditors and stockholders. If accepted and acceptances have not been made or procured by means forbidden by law an Order of Confirmation also issues as of course subject to the same general power reserved to the Bankruptcy Court, but if rejected the statute says "the judge may nevertheless confirm the plan if he is satisfied and finds after hearing—

(i) that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it;

(ii) that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and

(iii) that the Plan conforms to the requirements of Clauses (1) to (3) inclusive of the first paragraph of this sub-section (e)."

(The numbers (i), (ii) and (iii) are not in the text and are inserted for clarification and convenience in reference.)

So the Questions to be decided as limited by the *certiorari* as granted are:

First: Does the Plan of Reorganization as confirmed by the District Court make adequate provision for fair and equitable treatment for the interests and claims of the Debtor's General Mortgage Bonds?

Second: Was the rejection of the Plan by the General Mortgage Bondholders reasonably justified in the light of their respective rights and interests and all the relevant facts?

Third: Was the Plan one which the District Court was authorized to approve as meeting the requirements of Clauses (1), (2) and (3) of the first paragraph of sub-section (e)?

Incidental to these general questions are specific constitutional questions to which at the proper points the Court's attention will be directed.

Unless traditional rules of statutory construction are inapplicable in proceedings under Section 77 the required findings (i) and (ii) should be held to be in addition to and wholly distinct from the findings required by (iii) which is a reaffirmation of the findings required as the basis for the Court's Order of Approval. The apparent purpose of this requirement for a reaffirmation of the earlier findings is two-fold (a) to give the District Court a *locus poenitentiae* —a privilege of which Judge SYMES did not avail—and (b) to reinforce and implement the equity rule that "it is

the rights of the parties, at the time the decree is rendered, that ought to govern the Court in rendering the decree." (*Randel* v. *Brown*, 2 How. 406, 423.)

Status of the Debtor

In view of the attitude of the Petitioners in the Circuit Court of Appeals it may be helpful for counsel for the Debtor to state their conception of the Debtor's functions under Section 77. It is a mistake to assume—as hostile counsel are prone to do—that the Debtor appears solely or even primarily as the representative of equity interests. It is the Debtor's position that it is charged by Section 77 with a statutory duty to develop, to file and to carry through the Interstate Commerce Commission and the Courts a Plan of Reorganization which conforms to the law of the land and is fair and equitable to all classes of security holders and that in so doing it is the lawful representative of all security holders and creditors at least to the extent that they are not otherwise directly represented in the proceeding. This is the view of Judge Hincks who has devoted much of his judicial life to the affairs of the New Haven Railroad Company. At a pretrial conference Judge Hincks said:

> "The New Haven, Debtor, as it appears to me is acting in a fiduciary capacity primarily for junior equities although perhaps in a broader sense for all the composit securities."

That this must be the true view seems very evident when it is considered that Section 77 is so drawn as to permit the Debtor to file and to carry through a Plan of Reorganization without the intervention at any stage of the proceeding of a *single* party. The fiduciary capacity to which Judge Hincks here refers underlies Paragraph (4) of sub-section (c) which makes it mandatory for the offi-

cers of the Debtor to disclose any information bearing upon the fairness of any Plan and it should be noted also that Paragraph (13) of the same sub-section provides that the Debtor shall have the right to be heard on all questions arising in the proceeding—not questions relating to the equity position but *all* questions.

Scope of Debtor's Brief

In the argument which follows, counsel for the Debtor will first deal with the questions set out above relating to the inadequacy of the provision for fair and equitable treatment for the Debtor's General Mortgage Bondholders and their justification for rejecting the Plan and will then discuss very briefly what counsel conceive to be the unlawful and inequitable impacts of the Plan of Reorganization upon property rights of the Debtor as protected by the law of the land.

Appendix A is a critical analysis of certain recent reorganization decisions rendered by this Court. This was prepared for use of the Congress in connection with pending legislation. We think these decisions are wrong and in the Debtor's Petition in No. 286 we ask that they be reconsidered. Since this Petition is being held by the Court our views as amplified in Appendix A are submitted for such consideration as this Court may deem appropriate.

SUMMARY OF ARGUMENT

I

The Plan of Reorganization for the Debtor (a) does not make adequate provision for fair and equitable treatment for the interests and claims of the Debtor's General Mortgage Bondholders and (b) its rejection by them was reasonably justified in the light of their respective rights and interests and of all relevant facts.

The argument under this heading is presented in two subdivisions (a) and (b) which are preceded by a brief analysis of the protective provisions of Section 77 which Congress must have assumed to be a constitutional substitute for the traditional safeguards of a public sale. A question is here raised and discussed as to the value of these protective provisions under the interpretation placed upon Section 77 by the Interstate Commerce Commission and the Courts. This question is further discussed in an analysis of certain decisions of this Court which was prepared by one of the Petitioner's counsel for the use of the Congress in connection with pending legislation and is annexed as Appendix A.

A

The Plan of Reorganization does not make adequate provision for fair and equitable treatment for the interests or claims of the General Mortgage Bondholders

The basic argument under this subdivision is that provision for fair and equitable treatment is not afforded the General Mortgage Bondholders because it is possible to give far better treatment *within* the valuation and *within* the capitalization prescribed by the Interstate Commerce

Commission and *without* a revaluation reflecting subsequent economic changes and the Debtor's enhanced earning power. It is argued that by reason of this patent defect in the Plan the Order of Approval given by the District Court was properly reversed and the proceeding referred back to the Interstate Commerce Commission for a new Plan regardless of the rejection of the Plan by the Debtor's General Mortgage Bondholders—such reference back being mandatory under subsection (e) of Section 77.

B

The rejection of the Plan of Reorganization by the General Mortgage Bondholders was reasonably justified in the light of their respective rights and interests and all the relevant facts.

The argument under this subdivision is an interpretation of the provisions of subsection (e) of Section 77 relating to rejection set out in three separately numbered parts (*ante*, pp. 3-4) and an explanatory statement of the intent and purpose of these provisions made by the late Joseph B. Eastman when Coordinator of Transportation to the President of the United States and the Seventy-Fourth Congress—the substance being that the limitation on the otherwise unconditional veto power of 33⅓% of any participating class is aimed at obstructionists trying to secure unduly preferential treatment and should not be otherwise construed. (Report of Joseph B. Eastman, Coordinator of Transportation to the President and the Seventy-Fourth Congress—H. D. No. 89.)

In support of the argument that the General Mortgage Bondholders were reasonably justified in rejecting a Plan of Reorganization giving them 10% treatment when they felt justly entitled to 100% treatment there are four separate specifications as set out or paraphrased below.

(1) *The Plan was based upon an obsolete record.*

It is here shown that 90% of the claims of the General Mortgage Bondholders were held worthless on the basis of a record which for practical purposes had been closed for many years and was formally closed May 20, 1941, and that a motion to reopen made May 1, 1943 to receive evidence of changed economic conditions had been denied contrary to the following authorities:

Ecker v. *Western Pacific Railroad Corporation*, 318 U. S. 448;

Group of Institutional Investors v. *Chicago, Milwaukee, St. Paul and Pacific Railroad Company*, 318 U. S. 523;

National Labor Relations Board v. *Phelps*, 136 F. 2d, 562;

Atchison, Topeka & Santa Fe Railway Company v. *United States*, 284 U. S. 248.

The following cases alleged to overrule *Atchison, Topeka & Santa Fe Railway Company* v. *United States* are distinguished:

United States, et al. v. *Northern Pacific Railway Company*, 288 U. S. 490 (1933);

St. Joseph Stock Yards Company v. *United States*, 298 U. S. 38 (1938);

Baltimore & Ohio Railroad Company v. *United States*, 298 U. S. 349 (1936);

Interstate Commerce Commission v. *Jersey City*, 64 S. Ct. Rep. 1129 (1944).

(2) *The Plan offered less than the impounded income applicable to the General Mortgage Bondholders.*

It is here shown that for a claim including contract interest amounting to $43,548,155 on which interest *pendente lite* in excess of all accruals on senior debt at contract rates

amounts to $9,389,418 the General Mortgage Bondholders are offered $4,353,816 in common stock—less than half of the impounded income.

(3) *A reasonable doubt had arisen as to the prior interpretation of Section 77.*

Here it is argued that the General Mortgage Bondholders were justified in rejecting a Plan giving them 10% treatment in common stock under an interpretation of Section 77 which the Judiciary Committee of the House of Representatives had said in its Report to the House of Representatives in recommending the passage of H. R. 4960—afterwards H. R. 31—was wrong and was resulting in "unbearable hardship" to various holders of railroad securities including "Denver & Rio Grande Western."

(4) *The Plan of Reorganization disregards the law of the land in its treatment of the capital stock of the Utah Fuel Company.*

Under this specification it is shown that the stock of the Utah Fuel Company in the par amount of $10,000,000 pledged under an underlying mortgage subject to withdrawal by junior lienors and preferred stockholders at $6,000,000 and *restrictively* pledged was given as a bonus to the underlying lienor without valuation and in violation of the conditions of the pledge. This is dealt with subsequently as a breach of trust constituting an independent ground for reversal of the Approval Order made by the District Court.

In concluding the argument under this section of the Brief it is urged that most of the infirmities in the Plan which are featured in the Opinions of Judges HUXMAN and PHILLIPS are common to the 16 pending cases set out in a foot-note, all of which are deemed discredited by the dissenting Opinion of the late Joseph B. Eastment in St. Louis Southwestern Reorganization, 249 I. C. C. 5 (p. 191).

II

The Plan of Reorganization attempts to destroy the property rights of the Debtor and its stockholders contrary to the intent and purpose of Section 77 of the National Bankruptcy Act, to rudimentary principles of natural justice, and to the law of the land.

In limine under this heading it is pointed out that by mandate of subsection (e) the proceeding must be referred back to the Interstate Commerce Commission to proceed anew under subsection (d) and it is noted that in recognition of this mandate the Opinion of the Circuit Court of Appeals expressly provides:

> "Nothing in this opinion shall prejudice or foreclose the rights of the parties to propose a new plan of reorganization or the power of the Commission to formulate, approve, and certify a new plan of reorganization in the light of any relevant facts presented to the Commission in any proceeding under 11 U. S. C. Sec. 205(d). It is so ordered."

It is argued that both the statute and the most rudimentary principles of natural justice entitle both the General Mortgage Bondholders and the Debtor to present and support a new Plan that will reflect recent radical changes in the National economy and the improved earning power of the Debtor's properties.

Reasons are here assigned showing why the Commission's valuation was arbitrary and the *fiat* of a non-judicial body and why any Plan based upon a valuation that would not give 100% treatment to the General Mortgage Bonds and a substantial participation for stockholders would be confiscatory. The latter include—

(a) radical lowering of long time money rates;

(b) permanent elevation of National income through intensified industrial activity;

(c) construction of mammoth steel plant at Geneva, near Provo, Utah;

(d) increased earning power incident to $43,000,000 of capital expenditures *pendente lite*;

(e) numerous other factors specified in the Opinion of Circuit Judge PHILLIPS;

(f) fixation of rights by principles of bankruptcy and subsection (1) of Section 77.

In support of (f) the following authorties are cited:

Sexton v. *Dreyfus*, 219 U. S. 348;

People v. *American Loan & Trust Company*, 172 N. Y. 371;

Merrill v. *National Bank of Jacksonville*, 173 U. S. 131;

Board of Commissioners of Shawnee County, Kansas v. *Hutley*, 169 Fed. Rep. 92.

In concluding this division of the argument it is urged that a fair revaluation of the Debtor's properties would require an over-all figure in excess of $205,000,000 and an illustrative Plan of Reorganization is outlined which without increasing the Commission's basic valuation beyond the additional capital reinvested in the property by the Court will make all creditors whole and provide a substantial equity for the Debtor's capital stock. This Plan contemplates either a judicial revaluation or a public sale of the capital stock of the Utah Fuel Company and an application of the proceeds of sale in accordance with the terms of the pledge. A sale divorcing the production of coal from its transportation is advocated in view of the Commodities Clause of the Interstate Commerce Act—49 U. S. C. A. Ch. 1. Sec. 1(8).

Conclusion

The Debtor asks that the reference of the proceeding back to the Interstate Commerce Commission under subsection (e) be approved and that the Plan as made and the principles underlying its making be accorded a plenary resurvey.

ARGUMENT

I

The Plan of Reorganization for the Debtor (a) does not make adequate provision for fair and equitable treatment for the interests and claims of the Debtor's General Mortgage Bondholders and (b) its rejection by them was reasonably justified in the light of their respective rights and interests and of all relevant facts.

Prior to the enactment in 1933 of Section 77 of the National Bankruptcy Act the lien creditor of a Railroad Company could not be divested of his lien nor a debtor of his property through a reorganization without the protection of a public sale which ordinarily included a judicially pre-determined minimum price.

Section 77 of the National Bankruptcy Act offered as an alternative a reorganization safeguarded *inter alia* by the following protective requirements:

First: The opinion of an independent administrative body—the Interstate Commerce Commission—that the Plan of Reorganization is fair and equitable and otherwise meets meticulous specifications for the protection of property rights.

Second: A judicial approval which cannot lawfully be given unless and until the Court is "satisfied" that every one of those meticulous specifications has been met.

Third: Acceptance by two-thirds of each class of creditors voting thereon, but subject to a limited exception aimed at extortion and designed to prevent, *not to confirm*, injustice.

Fourth: Confirmation *only* after such creditor acceptance and a terminal activation of the conscience of the Court.

It is our contention urged with the utmost deference that the first and second of these three safeguards are of little if any value under the interpretation placed upon Section 77 by the Interstate Commerce Commission and afterwards accepted by this Court; and in this contention we are fortified by a Report made retrospectively by the Judiciary Committee of the House of Representatives which framed the Section (Tr., fol. 262).

Our views on the questions of interpretation are elaborated in Appendix A.

Except as we refer to and rely upon Appendix A and the basic requirements of due process the discussion under this Point will be limited to an effort to preserve in its full integrity the third safeguard: the right of the security holders to protect themselves by rejection of a Plan. As was observed in our Brief opposing the issue of the writ of *certiorari*, the third safeguard, the very last trench in the security-holders' line of defense against confiscation of their property is under heavy assault by Reconstruction Finance Corporation, the Insurance Companies and a chain of some 1,000 or more Savings Banks throughout the United States all working together in these Section 77 proceedings. One of the enigmas of the times (and there are many such) is the willingness of these great fiduciary institutions to cooperate with and aid the Interstate Commerce Commission in breaking down the statutory and constitutional safeguards against the expropriation of private property.

(A) The Plan of Reorganization does not make adequate provision for fair and equitable treatment for the interests or claims of the General Mortgage Bondholders.

The Plan of Reorganization offers to the General Mortgage Bondholders 10% of their claim in common stock representing 10% of the total issue. To quote Circuit Judge PHILLIPS this is "harsh treatment." The most callous confiscationist would admit that this is "harsh treatment" and is inadequate provision for fair and equitable treatment if better treatment can be given without taking anything given under the Plan to those in a superior position. There is no serious claim that far better treatment is not practicable *within* the valuation and *within* the capitalization prescribed by the Interstate Commerce Commission and *without* a revaluation reflecting the changes in economic conditions and the Debtor's enhanced earning power. From a number of different sources it is possible vastly to improve the position of General Mortgage Bonds without a revaluation. These sources include the securities released by the retirement of First Mortgage Bonds of The Rio Junction Railway Company, the securities released by the retirement of Equipment Trust Obligations and uncapitalized cash in excess of the working capital contemplated by the Plan. The facts as to these possible provisions for better treatment for junior debt are not in dispute and their existence puts the case outside of the sole exception to the unqualified right of veto given to one-third of the voters in any class to which a Plan is submitted. The Approval Order of the District Court having been reversed the proceeding was referred back to the Interstate Commerce Commission by the Circuit Court of Appeals under mandate of sub-section (e) of Section 77 to proceed anew without the necessity of a decision—which it nevertheless made and now to be discussed—that the rejection of the Plan of Reorganization by the General Mortgage Bondholders met the statutory test of reasonableness.

(B) The rejection of the Plan of Reorganization by the General Mortgage Bondholders was reasonably justified in the light of their respective rights and interests and all the relevant facts.

The Petitioners argue that rejection of a fair and equitable Plan of Reorganization can never be reasonably justified; that if the Plan is fair and equitable it cannot be altered to improve the position of a rejecting class without taking something from another class and thereby throwing the equities out of balance. If this be true the statutory provision set out *ante* pages 3-4 for rejection which we have numbered (ii) is a meaningless one because it is overlapped by the provisions which we have numbered (i) and (iii). Their argument is faulty both legally and factually; it is bad legally because it violates the cardinal rule that effect must be given to every clause of a statute; it is wrong factually because under the preceding head-note we have cited a number of factors which come into play in this very case to make possible substantially better treatment for the General Mortgage Bondholders than is given by the Plan without taking anything from anybody and without throwing any equity out of balance.

There may, however, be a multitude of relevant facts which reasonably justify rejection of a Plan of Reorganization which has been found to be fair and equitable by the Commission and the Court. Adequate provision for fair and equitable treatment is a *sine qua non* of a valid Plan before it even may be submitted for acceptance or rejection by parties in interest. So the statute necessarily contemplates an area of disagreement in which the veto of such a Plan by a vote in excess of 33⅓% of any class is absolute. Sub-section (e) delimits this area and we think that it does so aptly and effectively. But the late Joseph B. Eastman, who as Coordinator of Transportation sponsored the amendatory Section 77, explained this clause lucidly in a communication to the President and the Seventy-Fourth

Congress printed as H. D. No. 89, from which we briefly quote:

> "Arbitrary compulsion of plans over the dissents of the interested classes is not intended, nor is it believed that the courts will override strong dissents by any large number of such classes, or by a single large class, excepting where it is established that they have no interest in the property. Rather, the purpose is to prevent the obstruction of plans which are favored by the larger classes of creditors or shareholders, but which are obstructed by minorities in the smaller classes in the attempt to secure unduly preferential treatment."

The General Mortgage Bondholders are not obstructionists trying to secure unduly preferential treatment.

They are acting advisedly within the prescribed area of permissible disagreement to say that they do not accept the Plan which gives them 10% treatment when they should be given 100% treatment. They say this for a number of valid reasons, any one of which reasonably justifies their rejection of what the Interstate Commerce Commission has offered them.

We shall refer briefly to those which impress us as worthy of emphasis. There are many others that will suggest themselves to this Court after reading the mutually supplementary Opinions of Judges HUXMAN and PHILLIPS.

(1) The Plan was based upon an obsolete record.

The record in the Interstate Commerce Commission was closed on May 20, 1941. On May 1, 1943, the Debtor filed a Petition for leave to offer proof of changed economic conditions and operating results and of assets realized subsequent to May 20, 1941. The Petition alleged:

> "The Debtor, if afforded an opportunity to do so by this Commission, is prepared to show by evidence

> which it believes will prove to be of the most convincing character that since the close of the hearings in this Commission a greatly increased earning power has been developed much of which is in no way connected with the War or the War economy and is so far of a permanent and durable nature that it could not properly be ignored in an appraisal of the Debtor's properties and earning power for the purpose of said Section 77" (Tr., fol. 734).

This Petition was filed in the light of what was said in the Opinions of this Court in the *Western Pacific* and *Milwaukee* cases as to the setting aside of a Plan which is shown by evidence to have become unfair and inequitable by reason of changed conditions. These Opinions show a very clear recognition by this Court of the right of an injured party to require that a Plan be set aside in such circumstances. In neither of those cases, however, had there been an application to the Interstate Commerce Commission of the character set out above and what was said in those cases related only to such changes in economic conditions and the consequences thereof as at that early period of the changing cycle were within the necessarily narrow and restricted judicial knowledge of this Court.

The Court's vision was then obscured by the fog of a depression which was rising but had not yet lifted.

The Interstate Commerce Commission ignored the Debtor's Petition up to the time of the release of its Third Supplemental Report dated June 14, 1943, in which appears the following uninformative reference:

> "We have denied the Debtor's request for a further hearing filed on May 1, 1943."

At the same time the Commission made an Order also dated June 14, 1943 formally denying the Debtor's Petition on the unrevealing ground—

> "that additional evidence of the nature referred to in the Debtor's Petition filed on May 1, 1943, is not

required for a determination of the matter involved in a further modification of the aforesaid Plan of July 18, 1942" (Tr., fol. 739).

In the Debtor's Objections to the Plan of Reorganization as certified to the District Court by the Interstate Commerce Commission in its Third Supplemental Report the Debtor states:

> "*In limine* the Debtor objects to any consideration by the District Court of the Plan of Reorganization certified as aforesaid to the Court by the Interstate Commerce Commission on the ground that the Commission's determination was made without a hearing of the character required by the Fifth Amendment to the Constitution of the United States and is in effect an attempt to take the Debtor's property without due process of law and without observing due process as provided by Section 77 of the National Bankruptcy Act.
>
> "Specifically the Debtor excepts to and objects to a denial of the Debtor's petition filed with the Commission on May 1, 1943, a copy of which is hereto annexed and made a part hereof; and the Debtor hereby moves for an order by this Court referring this proceeding back to the Interstate Commerce Commission to receive evidence of the character outlined therein and for proceedings in accordance with the Statutes of the United States" (Tr., fol. 742).

The Debtor contends and respectfully asks this Court to hold that the Commission's denial of the Debtor's Petition filed May 1, 1943 if not a denial of due process was an abuse of discretion which alone required judicial disapproval of the Plan.

In Circuit Judge HUTCHESON's note to his Opinion in *National Labor Relations Board* v. *Phelps*, 136 F. 2d, 562, the learned Judge uses the following striking language:

> "Regulatory Commissions have been invested with broad powers within the sphere of duty assigned

> to them by law. Even in quasi-judicial proceedings their informed and expert judgment exacts and receives a proper deference from courts when it has been reached with due submission to constitutional restraints. Indeed, much that they do within the realm of administrative discretion is exempt from *supervision* if those restraints have been obeyed. All the more insistent is the need, when power has been bestowed so freely that the 'inexorable safeguard' of a fair and open hearing be maintained in its integrity. The right to such a hearing is one of 'the rudiments of fair play' assured to every litigant as a minimal requirement. There can be no compromise on the footing of convenience or expediency or because of a natural desire to be rid of harassing delay, when that minimal requirement has been neglected or ignored."

Reference must here be made to the following language of retired Chief Justice HUGHES in *Atchison, Topeka & Santa Fe Railway Company, et al.* v. *United States, et al.*, 284 U. S. 248:

> "In the instant proceeding, the hearing accorded related to conditions which had been radically changed, and a hearing, suitably requested, which would have permitted the presentation of evidence relating to existing conditions, was denied. We think that this action was not within the permitted range of the Commission's discretion, but was a denial of right. The order of the Commission which was thus made effective, and the ensuing supplemental order, cannot be sustained."

The case last cited (herein called the *Atchison* case) is a parallel one which cannot possibly be distinguished.

There has been no effort to distinguish it but it is said to have been overruled by the cases cited below.* Without

* *United States, et al.* v. *Northern Pacific Railway Company*, 288 U. S. 490 (1933); *St. Joseph Stock Yards Company* v. *United States*, 298 U. S. 38 (1938); *Baltimore & Ohio Railroad Company* v. *United States*, 298 U. S. 349 (1936); *Interstate Commerce Commission* v. *Jersey City*, 64 S. Ct. Rep. 1129 (1944).

undertaking to deal separately with each of these cases we ask this Court to note the following features:

(a) All of the cases, even the *Atchison* case, were *rate* cases where there is no finality and a new complaint may be filed at any time based upon changed conditions.

(b) In all of these cases, except the *Atchison* case, the petition was for a technical reargument to set aside an order already made and was not an application to permit the introduction of supplementary evidence in a pending proceeding in order to bring up to date a record that was stale and notoriously obsolete.

(c) In none of the later cases is it questioned that the *Atchison* case is a binding authority in any subsequent case where the basic facts are identical and the abuse of discretion is manifest.

(d) In the last of the cases the Court was dealing primarily with the normal lag or gap between the closing of the record and the time the administrative decision is promulgated. It is quite appropriate in such a case that the question of reopening the record in order to bridge the inevitable normal lapse of time should be left to the discretion of the administrative body.

But that is not our case.

Here the record had been closed for a period of approximately two years in which had occurred a world-wide economic upheaval without precedent in history and in which earning power of industry in general and of our transportation systems in particular had risen to undreamed of levels, much of the increased earning power being the result of factors that may readily be shown to be of a permanent nature. No true estimate of the Debtor's earning power could possibly be made without exploring all of these new factors at an open, unrestricted hearing in the Interstate Commerce Commission and without giving ef-

fect to evidence which such a hearing may develop.† If an irremediable forfeiture, such as is abhorred by equity, of property rights running into many millions of dollars might be averted by a further hearing such a hearing becomes mandatory under the letter and spirit of *Atchison, Topeka & Santa Fe Railway Company, et al.* v. *United States* which we think applies in its full vigor unaffected or unimpaired by anything said in the subsequent opinions. We do not think *Atchison, Topeka & Santa Fe Railway Company* v. *United States* has been overruled—indeed "the rudiments of fair play" (to re-quote Judge HUTCHESON) which underlie that decision may well be beyond the reach of judicial abrogation. But regardless of whether the arbitrary action of the Commission constitutes "a denial of right" (again to quote former Chief Justice HUGHES) it certainly "reasonably justified" the General Morfgage Bondholders in rejecting a Plan of Reorganization which deprived them of all but 1% of their investment knowing as they must of known that a fair reappraisal on the basis of newly developed but heretofore undemonstrated earning power would have made them whole and placed below them a valuable supporting equity.

(2) **The Plan offered less than the impounded income applicable to the General Mortgage Bondholders.**

If one should recklessly drive to death a post horse hired for a journey to Market Harborough and should offer the owner in settlement for the entire loss a sum actually 50% less than the amount stipulated to be paid as hire for the horse and not one farthing for the horse, that offer would parallel this case. Incredible as it may seem, the General Mortgage Bondholders are offered for their claims amounting with contract interest as of January 1, 1943, to $43,548,'55 common stock in the par amount of $4,354,816 whereas on August 1, 1944, which is the nearest date to the hearing on

† Certain of these factors are developed in a section of the Opinion of Circuit Judge PHILLIPS quoted herein—*post*, page 34.

Confirmation the accumulated income earned *pendente lite* in excess of all contract interest on prior lien debt amounted to $9,389,418, more than double the amount offered in common stock for the whole claim. While the impounded income may not be available to the General Mortgage Bondholders in cash because properly applied in reduction of principal of senior lien debt or prudently reinvested in the property such reduction of the prior lien debt or prudent reinvestment necessarily increases by that precise amount the securities available in reorganization for junior debt. It is difficult to understand how an offer of $4,353,816 in common stock on a lien claim of $43,548,155 on which income earned *pendente lite* in excess of interest accruals on prior debt amounts to $9,389,418* is an honest Plan much less a fair and equitable Plan; it is impossible to understand how it could be judicially determined that a rejection of such a Plan by the lien creditors thus victimized was not "reasonably justified."

(3) **A reasonable doubt had arisen as to the prior interpretation of Section 77.**

The Plan of Reorganization under which holders of General Mortgage Bonds were to be accorded 10% treatment in common stock representing only 10% of the proposed issue was pending for their acceptance or rejection under sub-section (c) of Section 77 when the Judiciary Committee of the House of Representatives released its unanimous Report (No. 1615) recommending passage of H. R. 4960 in which the Judiciary Committee said in the opening paragraph:

> "The purpose of the bill is to correct a very serious situation arising from the interpretation placed by the Interstate Commerce Commission and the Courts upon amendments of Section 77 enacted by Congress August 27, 1935. We believe this situation results from a misapprehension of the intention of Congress with respect to the 1935 amendments. The consequences have been and are so disastrous to rail-

* The amount shown in City Bank Farmers Trust Company Ex. 10 at folio 382 of the Transcript—$9,779,021—is partially estimated. The final figure is as stated above.

road investors and so dangerous to the credit of the railroads in general that they should be corrected by legislation" (Tr., fol. 262).

This is followed by examples which this situation created of "unbearable hardship" upon junior investors in railroad securities. Among those specifically mentioned is "the Denver & Rio Grande Western." It was therefore not surprising that four out of every five holders of General Mortgage Bonds rejected the Plan. It is an understatement to say that they were "reasonably justified." Rejection was an obvious duty from which no well informed General Mortgage Bondholder could escape.

4. The Plan of Reorganization disregards the law of the land in its treatment of the capital stock of the Utah Fuel Company.

Many questions of grave import arise out of the dispositive provisions of the Plan of Reorganization respecting the capital stock of the Utah Fuel Company. Here again appear relevant facts which taken alone constitute adequate justification for rejection of the Plan by General Mortgage Bondholders. By methods of doubtful constitutionality plainly violative of valid contract reservations the General Mortgage Bondholders are to be divested of a valuable equity in this *restrictively* pledged stock which is given away by the Interstate Commerce Commission either without valuation or at an undisclosed valuation as a bonus or sweetening gratuity to a group of prior lien creditors who appear already to have been made whole under their Plan. This factor also constitutes an independent legal ground for judicial disapproval of the Plan without regard to its subsequent rejection by the General Mortgage Bondholders and in this aspect will be discussed at a subsequent point. References to the stock of the Utah Fuel Company in the Reports of the Interstate Commerce Commission and to the basic documents are set out below.*

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* Submission Pamphlet—pp. 38, 52, 53, 70, 77, 78, 123, 135, 136. Tr. fols. 1541-1557; Exhibits 34, 34J, 35, 36, 37A; fols. 1496, 1498, 1525.

The Utah Fuel Company owns and operates coal mines in the region of Provost near Salt Lake City, Utah; its coal reserves underlying the Wasatch Range of the Rocky Mountains have been scarcely scratched in its successful operations extending over a period of nearly 50 years. By reason among others of the quality and accessibility of this vast reserve of coal the United States Government has constructed near Geneva in the environs of Provo and at the very portals of these mines, the largest and most modern steel plant now in existence at a cost exceeding $200,000,000 which is far greater than what appears to be the Commission's notion of the value of the entire Denver and Rio Grande Railway System.

This plant was constructed after the formulation of the Plan of Reorganization which the General Mortgage Bondholders have rejected and the Circuit Court of Appeals has set aside.

In the depression year of 1935 the Utah Fuel Company had earned $83,000 when many of the strong units of the coal industry throughout the United States were running large deficits and a number were in receivership or reorganization (Poor's 1937 Industrial Volume, pp. 1635-1636; 1802, 2208). In 1943 after the depression had receded and the Geneva steel plant had been put into production the earnings had reached the approximate level of $1,000,000 representing more than a ten-fold increase over 1935. (Tr., fols. 1102; 1460).

The capital stock—$10,000,000 par value, all common shares—had been pledged as part security for First Consolidated Mortgage Bonds of the Rio Grande Western Railway Company (one of the Debtor's early constituents) in the amount of $15,080,000. The pledge of the stock under this underlying mortgage was made by a supplemental indenture executed by Messrs. Spencer Trask and Company, New York bankers, a number of years after the execution of the original mortgage. The pledge was subject to an

expressly reserved right of release and withdrawal of the stock upon deposit with the mortgage trustee of $6,000,000 which happened to coincide with the principal amount of First Consolidated Mortgage Bonds simultaneously issued to the bankers. The rights of withdrawal and redemption and ultimate equity of and in the stock were afterwards transferred by legal proceedings not here material to the present owners of the common capital stock of the Debtor, The Denver and Rio Grande Western Railroad Company. This subsequent transfer was subject in all respects to the liens in the order of their respective priorities of the two junior mortgages securing Bonds of the Debtor to which participation is accorded by the terms of the Commission's Plan of Reorganization—these being the Refunding and Improvement Mortgage and the General Mortgage. The present rights of the various parties in interest are set forth in certain agreements referred to in the last foot-note, one of which provides (reversing the rule applicable to accommodation collateral) that the Utah Fuel Company stock must be liquidated and applied to the payment of the First Consolidated Bonds before there can be a resort to other mortgage security.

In the formula which the Interstate Commerce Commission says it used in its formulation of the Plan of Reorganization an income of $83,000—the amount accruing in the depression year 1935—was credited to the First Consolidated Mortgage as one of the factors in its determination of the amount and character of securities to be allotted to holders of First Consolidated Mortgage Bonds. In addition, however, all of the stock of the Utah Fuel Company or the proceeds of sale (if the mortgage trustee elects to sell) are given outright to the holders of First Consolidated Mortgage Bonds and all rights of junior lienors, one of which is the Debtor's General Mortgage, are disregarded. It ought to be clear that this is fundamentally wrong. The very least that could be done correctively would be to credit the fair value—not the depression value—of the Utah Fuel

Company in reduction of the claim of the First Consolidated Mortgage Bondholders. The effect of such credit would be to pass the amount thereof down to the highest ranking junior lienor not already made whole and this would be the General Mortgage which is given $4,354,816 in common stock for a claim asserted in the amount of $43,548,155.

This brings up the more critical constitutional question—how is the fair value of the Utah Fuel Company to be determined in accordance with the law of the land. Discussion of this question will be reserved for a subsequent point. It is sufficient here as justifying the adverse vote of the General Mortgage Bondholders to note with appropriate emphasis that a capitalization of earnings at the 1943 level—presumptively the permanent level—using the unjustifiably high rate of 5% would indicate a value of approximately $20,000,000, all of which should be carried down to the General Mortgage Bondholders.

To multiply further the relevant facts which reasonably justify the rejection of the Plan of Reorganization promulgated for the Debtor would unduly extend this Brief. Sufficient has been shown to condemn the Plan utterly and completely. It should be emphasized, however, that the Plan for the Debtor is fairly typical of those for sixteen pending cases to which the Interstate Commerce Commission is in principle committed. As early as June 30, 1941, the late Joseph B. Eastman, then Chairman of the Interstate Commerce Commission and soon to be made Director of the Office of Defense Transportation, had reached the conclusion that much of the increased carrier revenue was of a permanent nature and that Plans of Reorganization on the Commission's pattern could no longer be justified.* In no subsequent case, so far as we have been able to determine, did Commissioner Eastman approve of or concur in any Commission Plan which con-

* St. Louis Southwestern Railway Company Reorganization, 249 I. C. C. 5, at 191.

fiscated the equity on the basis of pre-war depression earnings. In the sixteen cases now pending the aggregate of the securities representing the equity of the stock is $1,162,062,000.† Most of the infirmities in the Plan of Reorganization of the Debtor which are featured in the Opinions of Judges HUXMAN and PHILLIPS are in some form or other common to the pending Section 77 cases, all of which should be referred back to the Interstate Commerce Commission for reconsideration. A list of these cases is shown below.*

II

The Plan of Reorganization attempts to destroy the property rights of the Debtor and its stockholders contrary to the intent and purpose of Section 77 of the National Bankruptcy Act, to rudimentary principles of natural justice, and to the law of the land.

Under the previous point we have attempted to show (we think successfully) that the Plan of Reorganization does not make adequate provision for fair and equitable treatment for the interests and claims of the Debtor's Gen-

† Since this calculation was made the Plan of Reorganization for the Chicago, Milwaukee, St. Paul and Pacific Railroad Company has been consummated by delivery of the new securities and the elimination of the equity of its stockholders appears to be a *fait accompli*. This is not therefore treated herein as a pending proceeding although an appeal has been taken from an Order denying a motion for a modification of the Decree pursuant to which the new securities have been issued.

* Alton
Central of Georgia
Central Railroad of New Jersey
Chicago, Indianapolis & Louisville
Chicago, Milwaukee, St. Paul and Pacific Railroad Company
Chicago, Rock Island & Pacific
Denver & Rio Grande Western
Duluth, South Shore & Atlantic
Florida East Coast
Missouri Pacific Lines
New York, New Haven & Hartford
New York, Ontario & Western
New York, Susquehanna & Western
Rutland
St. Louis-San Francisco
St. Louis Southwestern Lines

eral Mortgage Bondholders. If this has been demonstrated it then follows under the clear mandate of subsection (e) that the proceeding must be referred back to the Interstate Commerce Commission for a new Plan which goes forward in accordance with subsection (d). It is in recognition of this statutory mandate that the Opinion of the Circuit Court of Appeals expressly provides—

> "Nothing in this opinion shall prejudice or foreclose the rights of the parties to propose a new plan of reorganization or the power of the Commission to formulate, approve, and certify a new plan of reorganization in the light of any relevant facts presented to the Commission in any proceeding under 11 U. S. C. Sec. 205(d). It is so ordered" (Tr., fols. 261-262).

One of the obvious rights of the General Mortgage Bondholders upon such a reference back is the right to file a new Plan of Reorganization for the Debtor and to endeavor to support it by evidence which—

> (a) will reflect the true present day value of the Debtor's properties;
>
> (b) will make the General Mortgage Bondholders whole; and
>
> (c) will provide for the largest possible junior equity to support and give the maximum permissible margin of safety for the new securities to be issued to the General Mortgage Bondholders under the new Plan.

The same right in the Debtor to file and support by evidence of present day values a Plan that will give due recognition to the Debtor and its stockholders is implicit in the same two subsections of Section 77.

There is nothing in either subsection (d) or subsection (e) to indicate a Congressional intent that the Debtor may be put out of the proceeding *pendente lite* and permanently

deprived of property rights for which a value might be established by economic changes and by huge accumulations of cash and impounded income developed during the further progress of the proceeding to final decree.†

Equity which abhors a forfeiture could not well forfeit property rights on the basis of an interlocutory judgment.

Even if the permanent elimination of the Debtor at a preliminary stage of the proceeding had been contemplated by Congress (which we submit was not the case) it would offend rudimentary principles of natural justice, shock the conscience, and violate the law of the land to exclude the Debtor in the present proceeding from further participation by reason of a death sentence imposed in a period of hysteria upon a record which was unsound in its inception and has become obsolete as the result of a new economy.

A brief summary of the Debtor's complaints ought to be sufficient to end the argument.

The reproduction cost less accrued depreciation of the Debtor's road and equipment arrived at by methods approved by this Court were shown to be not less than $205,000,000 at the hearing in the District Court held July 29, 1940 (Tr., fols. 1259-1260). This valuation of physical elements does not reflect—

(a) common stock of the Utah Fuel Company $10,000,000-$20,000,000 (Tr., fols. 1261; 1460);

(b) development cost at 5%—$10,000,000 (Tr., fols. 1257-1260);

† In an opinion of the Securities Exchange Commission released January 25, 1946, in the matter of the reorganization of the Commonwealth and Southern Corporation it is stated:

"Market valuations are higher than when the plan approved by the SEC was filed. It would be unfortunate to cut off finally any appreciation which common stockholders might realize as a result of improved future earnings, prospects and market conditions.

"Careful consideration should be given to the possibility that a change in the form of reorganization might preserve larger interest for common stockholders, while fully satisfying the claims of preferred stockholders."

(c) nor present day prices at least 20% above those of 1940—$41,000,000.*

These are but a few of many elements of *added* value to which due process requires that a court of equity give heed.

The Debtor's investment in road and equipment at the same date was greatly in excess of $205,000,000 (Annual Report, 1935, p. 12).

This understates by many millions of dollars the present value of the property of the Debtor devoted to public service upon which it is guaranteed the right to earn a fair return by the Fifth Amendment.

A fair revaluation of the Debtor's property on the basis of the present day prices and altered economic conditions to which we think the General Mortgage Bondholders as well as the Debtor are indubitably entitled would support a new capitalization well above $205,000,000 unless the value of the physical elements may lawfully be written down in a proceeding under Section 77 by a capitalization of the undisclosed guess of an administrative Board as to the Debtor's earning power. It is the view of Debtor's counsel that the value of the Debtor's property devoted to public service cannot be written down for reorganization purposes under Section 77 as is here proposed. The protection of a public sale at which interested parties may become bidders should not be lightly put aside; but if it is to be put aside—and, rightly or wrongly (we think wrongly), this seems to be the trend in proceedings under Section 77—the evidence in justification of radical reductions proposed for the purpose of excluding the Debtor should be clear and convincing and when translated into the finding of an administrative Board should be fully and fairly disclosed so as to be susceptible of evaluation by and an adequate review in the Courts.

* In a Petition dated October 5, 1944 filed by the Rail Carriers in the Interstate Commerce Commission in *Ex Parte* 148 it is stated: "Since 1940 railway labor and costs have increased approximately 27% and the price of materials and supplies required by the Railroads have advanced an average of 29%."

The valuations alleged to have been made by the Interstate Commerce Commission in the pending proceeding fail to meet such a test.

If, as is claimed, these valuations are based upon a capitalization of future earnings the Debtor is left in ignorance of the two basic factors—first, it is left in ignorance as to the amount of the estimated annual income which the Commission has capitalized; and second, it is left in ignorance as to the interest rate which was used by the Commission as the basis of the computation. Since these factors are not disclosed the Debtor's properties are being taken away arbitrarily by *fiat* of an administrative Board and for that reason alone the Debtor is entitled to have the proceeding set aside and its properties revalued. Such right of revaluation exists by reason of the methods pursued by the Interstate Commerce Commission and is distinct from and independent of the right of the Debtor to a revaluation as incident to the subsequent economic changes which have rendered obsolete and unjust the Commission's earlier valuations even if they were fair when made which we respectfully submit they were not.

This brings into the foreground an impressive reason why *all* of the fifteen cases pending under Section 77 should be remanded to the Interstate Commerce Commission for reconsideration: in all of them the Commission's Plans have become unfair and inequitable by reason of recent economic changes which are revolutionary.

One of these changes is the radical lowering for the indefinite future of money rates.

The Plans in the fifteen cases pending (with only minor exceptions) assume 4% to be the minimum interest rate for new interest bearing securities to be issued in reorganization. In most cases a higher rate is provided for at least a part, if not all, of the new debt. The minimum assumed rate of 4% is now down to 3% as an incident of the change in the National economy. The trend is shown by the sub-

joined foot-note.* The New York Times (February 5, 1946) reports a sale by the Southern Pacific Railroad Company of $50,000,000 of First Mortgage 2⅞% Bonds at 100.6599 to replace Bonds issued less than six months ago bearing interest at 3¾%. The New York Times (February 7, 1946) reports a sale by Union Pacific Railroad Company of $44,193,000 of Thirty-Year 2⅞% Debenture Bonds having no lien at all at 108.50. Economists will testify (if they are permitted to do so) that the National economy requires that money rates be stabilized at an even lower rate. It is quite evident therefore that a revaluation of the properties of each of the fifteen unreorganized carriers would require an earning factor very much above that upon which the Plan is based even though it be assumed that there will be no higher income than was estimated in the period of the depression.

In most of the pending cases (and this is conspicuously true in the case of the Debtor) there are other new factors which permanently elevate earning power to a level far above that which could possibly have been estimated or predicated upon historical or current earnings.

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*STATEMENT SHOWING CHANGES IN INTEREST RATES REFLECTED BY RECENT REFINANCINGS OF RAILWAY LIEN INDEBTEDNESS

Name	*Date of Refinancing*	*Interest rate of old issue*	*Interest rate of new issue*
Chicago, Burlington and Quincy RR. Co.	Aug. 1–Dec. 1, 1944	4–5%	3½% 1½% 3¾%
Chicago and Northwestern Railway Co.	Jan. 1, 1945	4%	3%
Chicago Union Station Company	July 1, 1944	3½%	2⅝%
Erie Railroad Company	Oct. 1, 1944	3¾%–4%	3¼%
Great Northern Railway Company	July 1, 1944	4–4¼%	3¼–3½%
Great Northern Railway Company	July 1, 1945	3¾%–4½%	3⅛%
Louisville and Nashville Railroad Co.	Oct. 1, 1944	3½–3½%	3⅜%
Pennsylvania Railroad Company	Jan. 1, 1945	4½%	3⅛%

Foremost among these factors—and this is common to all of the fifteen cases—is the permanent elevation of National income. In order to service our great National debt it is a problem of the Government to maintain National income at an incredible level and it is almost *lese majeste* to assume that the Government will fail to achieve this result. Economists will also testify (if permitted so to do) that the industrial activity and expansion necessary to achieve such a National income would involve demands upon all forms of transportation even in excess of those created by the exigency of the War. This factor alone should preclude the use of historical or pre-war earnings to write down a Debtor's property investment as protected by the law of the land.

The Denver and Rio Grande Western System is, it should be added, in a peculiarly strong position to benefit by the new National economy. The more important reasons for this are summarized in the Opinion of Circuit Judge HUXMAN and are elaborated in the Opinion of Circuit Judge PHILLIPS. The attention of this Court is respectfully directed at this point to the following section of the Opinion of Circuit Judge PHILLIPS:

"Approximately $43,000,000 of the income available, but not used, for the payment of interest has

Name	*Date of Refinancing*	*Interest rate of old issue*	*Interest rate of new issue*
Pere Marquette Railroad Company	Mar. 1, 1945	4-5%	3⅜%
Union Pacific Railroad Co.	Oct. 1, 1944	4%	3%
Wabash Railroad Company	Feb. 1, 1945	4%	3¼%
Washington Terminal Co.	Feb. 1, 1945	3½-4%	2⅝%
Erie Railroad Company	Jan. 1, 1945	4%	3⅛%
Erie Railroad Company	Mar. 15, 1945	3⅛%	2%
Reading Company	Apr. 1, 1945	4-5%	3⅛%
New York Connecting RR.	Oct. 1, 1945	3½%	2⅞%
Lehigh & New England RR. Co.	Nov. 1, 1945	4%	3%
Western Maryland Ry.	Nov. 1, 1945	5½%	1¾%-3¼%
Pennsylvania Ohio and Detroit RR. Co.	Oct. 1, 1945	3¾%-4½%	2⅞%
Term. RR. Ass'n. of St. Louis	Oct. 1, 1945	3⅜%-4%	2⅞%

been expended in permanent improvements and betterments. While the investment value of the debtor's property thus was substantially increased, the Commission's valuation, based on estimated future earnings, was not increased proportionately. As a result, the claim of the senior security holders has increased and the participation of the general mortgage bondholders has been pressed downward until it is now fixed at 10 per cent of the new common stock. Many of the improvements and betterments referred to above, have substantially increased the capacity of the railroad to handle increased traffic as it arises. Central train control installed in many segments, where the greatest density of traffic obtains, gives to those segments, in a large degree, the equivalent of a double-track railroad and increases the number of trains that can be operated over the road and the volume of traffic that can be handled by the road. Other of such improvements have contributed to efficiency and economy in operations. These improvements have enabled the debtor to handle the great increase in traffic resulting from the war effort and have placed the debtor in a position to more economically and efficiently handle a volume of traffic largely in excess of its prewar traffic, should future economic conditions produce such traffic. Under the plan approved and confirmed by the district court, 90 per cent of the common stock goes to the holders of the senior securities and 10 per cent to the general mortgage bondholders. As a result, should there be a substantial increase in the debtor's postwar traffic over its prewar traffic, 90 per cent of the increased earnings will inure to the benefit of the holders of the senior securities and only 10 per cent to the general mortgage bondholders, whose claim was decreased 90 per cent by reason of the failure to discharge interest accruals with income available therefor and the diversion of such income to the cost of such permanent improvements. It seems to me, under all these circumstances, that, in addition to the other adjustments required to make the plan fair and equitable, the Commission should endeavor to modify the plan so as to give relief from the situation that lets the full impact of the improvement program fall

upon the claim of the general mortgage bondholders and accords them no corresponding benefits.

By confirming the finding of the Commission that the equities of the unsecured creditors and the stockholders are without value, based on an estimate of future earnings, an estimate at best shrouded in uncertainty, the court, by judicial fiat, has forever forfeited and destroyed the rights and interests of such creditors and stockholders in the assets of the debtor, a result which, under well-settled principles, a court of equity will ordinarily avoid.

It may be urged that the elimination of the stock will provide the debtor with a stronger financial structure and enable it to better serve the public interests, but private property cannot be taken in the public interest without just compensation.

Even if viewed solely from the standpoint of future earnings, it would seem that it should not be said such stock is without value merely because, during periods of receding economy and depression, the earnings of the debtor will not be sufficient, after payment of prior claims, to provide funds from which dividends on such stock can be properly paid. Such stock has value, if, during periods of expanding economy and prosperity, the earnings of the debtor will be sufficient to provide for prior claims and leave a surplus from which substantial amounts can be lawfully paid as dividends thereon; and a finding of no value should not be made if there is reasonable probability that earnings will be realized from which substantial dividends can be paid, even though only during periods of economic prosperity.

It seems to me, under the facts presented on this record and those of which we may take judicial notice, that it is not unlikely the estimate of future earnings of the debtor made by the Commission will fall far short of its actual future earnings. Should the estimated earnings prove to be substantially under the actual earnings, the injustice that will result to the holders of the general mortgage bonds and to the stockholders of the debtor is obvious.

It may be reasonably assumed that a substantial portion of the war industries contributing traffic to the road will be succeeded by permanent industries. For example, it is common knowledge that the Kaiser Industries and one of the large Eastern steel companies have indicated a desire to acquire and continue the operation of the Geneva Steel Plant, a large and modern steel plant built on the debtor's line of railroad. In the areas tributary to debtor's line of railroad, there is an abundance of cheap power and of fuel and ore. Many heavy traffic-producing enterprises have been and are being established in new areas tributary to the debtor's line of railroad. It is reasonable to believe that this industrial development will continue.

Furthermore, changes in national income at constant prices have an approximately constant relationship to changes in ton-miles of traffic. It may be said, in general, that traffic is so related to national income that when that income rises by one billion dollars, traffic rises by about 6.6 billion ton-miles. Certain federal agencies have made estimates of the national income for the years 1947 to 1949. These estimates predict a national income of approximately 135 billion dollars in 1947 and a rising national income in 1948 and 1949, reaching 150 billion dollars in the latter year.[3] This would indicate a postwar railroad traffic reaching in 1949 a level of that traffic during 1943.

Moreover, the ratio between ton-mile revenue of Class I railroads and the number of factory workers engaged in the production of durable goods is fairly constant. It is 100,000 revenue ton-miles for each factory worker. That there will be a determined effort to provide jobs for upward of 55 million workers early in the postwar period is a well-known fact. This indicates a greatly increased postwar railroad traffic. Moreover, the record demonstrates that, with the exception of a slight dip in 1923, the

[3] See Post-War Traffic Levels, prepared by Spurgeon Bell, Head Transport Economist, and I. E. Peabody, Principal Transport Economist, of the Interstate Commerce Commission, pp. 42-71, 90-114.

> debtor has been securing a constantly increasing proportion of the operating revenues of Class I railroads. If the debtor should enjoy postwar earnings approximating its 1943 earnings, it is clear that the valuation found by the Commission should be substantially increased."

The development and construction of the great steel plant at Geneva is alone a reason for a complete revaluation of the Debtor's properties and the formulation of a new Plan. The establishment of this industry on the Debtor's rails is certain to be revolutionary in its contribution to the new earning power of the Debtor's properties. Manifestly this and other things specified by Judge PHILLIPS should be the subject of scientific analysis and study and appraisal before there can be a fair and final determination either by an administrative Board or by a Court that the equity represented by the Debtor's stock is without value.

Let us here be specific because our properties are being taken from us upon the vaguest generalities.

The evidence shows and the Opinions of Judges HUXMAN and PHILLIPS each refer to capital expenditures made during the trusteeship aggregating more than $43,000,000 (Tr., p. 249; Annual Reports, 1935-1944). Only a negligible part of these expenditures had been made prior to the original valuation of the Debtor's properties by the Interstate Commerce Commission in its Report dated July 11, 1939 (Tr. 68; Annual Reports, 1936-1937). There was expert testimony of high quality that capital expenditures in the railroad industry are not deemed provident that yield an annual income rate below 10%. The witness said—

> "I spent several years with the Pennsylvania Railroad making economic studies of the savings it had out of new work, the added traffic to be obtained by new lines and extension of lines, and I know very well an improvement that didn't earn fifteen per

cent on its cost or was not estimated to earn fifteen per cent on its cost would receive no consideration whatever from the management, and I therefore assume that these improvements or most of them could be expected to earn ten per cent to fifteen per cent or even more in some cases" (Tr., pp. 316-317).

Applying the lower percentage an increased earning power of $4,300,000 is indicated as the result of the Court's capital investments. Capitalized at 4% this would increase the Commission's original estimate based on capitalizable earnings by adding thereto $107,500,000. This addition would increase the Commissions basic valuation of $147,717,268 made in its Report of July 11, 1939 to $254,717,268. To say that the Debtor's capital stock is worthless on the basis of a valuation made many years back and which frankly ignores this accretion to earning power alone condemns the Plan as both arbitrary and confiscatory.

There are other factors that lead to the same conclusion.

If it be assumed—and the assumption is a fair one—that the net income to be derived from new tonnage contributed by the steel plant recently constructed at Geneva combined as it should be with the increased net income furnished by the Utah Fuel Company would amount to only $2,000,000—and one-half of this is now being contributed by the Utah Fuel Company alone—and it be further assumed that this amount of increased net income is fairly capitalizable at 4%—and this is at least 1% above the current rate—there is an increase in capitalizable over-all value of $50,000,000. If the Commission's original valuation is increased to this extent the increase is sufficient under the Commission's Plan otherwise unchanged to make the General Mortgage Bondholders whole and provide a substantial equity for the Debtor's capital stock.

It is to be borne in mind that Section 77 is a part of the National Bankruptcy Act and so far as is consistent

with its purposes as a reorganization statute it should be administered in accordance with established bankruptcy principles.

One of the traditional bankruptcy principles coming over to us from England is that the rights of the parties are fixed as of the date of the filing of the petition and that the final decree relates back to the day when the Court took possession of the assets. On that day contracts end and the rights of the parties are *in rem*. In *Sexton* v. *Dreyfus*, 219 U. S. 339, in an opinion by Mr. Justice HOLMES this Court said at page 345:

> "If, under Section 57 of the present act, the value of the security should be determined by agreement or arbitration the time for fixing it naturally would be the date of the petition. At that moment the creditors acquire a right *in rem* against the assets. *Chemical National Bank* v. *Armstrong*, 59 Fed. Rep. 372, 378, 379. Merrill v. National Bank of Jacksonville, 173 U. S. 131, 140."

The philosophy of this rule is very fully developed by the decision of the Court of Appeals of New York in *People* v. *American Loan & Trust Co.*, 172 N. Y. page 371. We quote the following from the opinion in that case written by Judge VANN:

> "The process of administration provided by law is through a receiver, as the executive arm of the court. He is appointed for the benefit of all the creditors, both preferred and unpreferred, and holds the assets, under the direction of the court, in trust primarily for them and finally for the corporation or its stockholders. Thereupon by operation of law the creditors become the equitable owners of the assets and the administration of affairs is for their benefit as such . . .
>
> "As we said in a recent case, 'it is the day on which the court practically takes possession of the assets of the company for the purpose of distribution among its creditors and consequently (that) is the

day on which the rights of creditors should be ascertained and the value of their claims determined.' "

In *Merrill* v. *National Bank of Jacksonville*, 173 U. S. 131, it was pointed out by this Court that the Courts of the several States were not in agreement as to the precise time when jurisdiction of the bankruptcy court attached. Upon this point Chief Justice FULLER said:

> "In *Kellocks's* case, L. R. 3 Ch. App. 769, it was held that the creditor's interest in the general fund to be distributed vested at the date of presenting or proving his claim; and this rule has been followed in many jurisdictions where statutory provisions have been construed to require an affirmative election to become a beneficiary thereunder. For instance, the cases in Illinois construing the assignment act of that State, which are well considered and full to the point, hold that the interest of each creditor in the assigned estate 'only vests in him when he signifies his assent to the assignment by filing his claim with the assignee.' *Levy* v. *Chicago National Bank*, 158 Illinois, 88; *Furness* v. *Union National Bank*, 147 Illinois, 570.
>
> "On the other hand, the Supreme Court of Pennsylvania in *Miller's Appeal*, 35 Penn. St. 481, and many subsequent cases, has held, necessarily in view of the statutes of Pennsylvania regulating the matter, that the interest vests at the time of the transfer of the assets in trust."

In framing Section 77 of the National Bankruptcy Act Congress did not leave this question in doubt but with meticulous care and foresight it adopted and in subsection (l) *prescribed* for cases under Section 77 the rule that rights are fixed as of the date of the filing of the petition. This subsection provides:

> "In proceedings under this section and consistent with the provisions thereof * * * the rights and liabilities of creditors and of all persons with respect to the Debtor and its property shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

This established principle of bankruptcy and express provision of subsection (1) declaratory and confirmatory thereof has been disregarded in the pending proceeding to the manifest injury of the Debtor as well as its General Mortgage Bondholders.

As already shown the lowest valuation placed upon the Debtor's properties by the Interstate Commerce Commission based upon a record closed June 15, 1937, was $147,717,268.* There had been no substantial accretion to the *corpus* between that date and November 1, 1935, the date of the filing of the Petition (Annual Reports, 1936-1937). On November 1, 1935 the total amount of all claims of creditors secured by liens prior to the General Mortgage was $101,293,850, so that there was a trust estate sufficient to provide in full for all creditors having claims secured by such prior liens; to provide in full for $29,808,000 principal amount of General Mortgage Bonds and to provide an equity for the Debtor's stockholders in the amount of $16,615,418 (Annual Report, 1935, pp. 13, 34).

Let us repeat: the interests of the parties were fixed in these amounts by both the fundamental rule of bankruptcy long ante-dating subsection (1) and by subsection (1) and the law has been flagrantly violated.

In respect of the claim of General Mortgage Bondholders for principal in the amount of $29,808,000 *plus* their proportionate share of increment during trusteeship which without equitable adjustment was not less than $9,389,418 at the end of the calendar year 1944 these Bondholders are offered $4,353,816 in common stock and the equity of the Debtor's capital stock which stood at $16,615,418 on the date when the rights of all parties were fixed both by the

* The Commission has developed four different Plans which assume three different valuations:—Report July 11, 1939—$147,717,268; Report April 2, 1940—$147,717,269; Report July 13, 1942—$154,521,612; Report June 14, 1943—$155,173,127 (Transcript, pp. 68, 106, 124, 156). Our references to these assumed valuations in this Brief must not be construed as an admission that they are valid or conform to due process. We contend otherwise.

bankruptcy rule and by subsection (1) is declared to be worthless.

This might indicate that the property had depreciated during trusteeship but such is not the case. Subsequent to basic date not less than $43,000,000 of earned income had been invested in the property in the process of judicial administration. The earned income exceeded the accumulation of contract interest on senior debt and greatly exceeded what a court applying bankruptcy principles could be expected to allow such creditors in lieu of contract interest, and it will now be in order to discuss the income problem.

As shown by the authorities cited above it is a basic principle of bankruptcy confirmed for cases under Section 77 by subsection (1) that rights are fixed as of the date when the bankruptcy court takes judicial custody of the *res* and as a corollary interest as such ceases to accrue on that date.

As between creditors themselves therefore there is no accumulation of interest *pendente lite*. In the final adjustment an equitable participation in any increment or accretion to the trust estate in excess of the principal of creditor claims is allowed each creditor and we think a just and equitable rule requires the division to be made at a uniform rate. In England by the Act of Parliament adopted in 1883 a uniform rate of 4% is provided. The pertinent text follows:

> "(4) Subject to the provisions of this Act all debts proved in the bankruptcy shall be paid pari passu.
>
> "(5) If there is any surplus after payment of the foregoing debts, it shall be applied in payment of interest from the date of the receiving order at the rate of four pounds per centum per annum on all debts proved in the bankruptcy."
>
> (Law Reports, 46-47 Viet., 1883, Statutes Vol. 19, Ch. 52, Sec. 40, Subsec. 4 and 5.)

There is a question whether the rate should be frozen as it has been by Parliament. Interest rates are too volatile and respond to too many changing factors. The creation of a great National debt as has been done in England as well as here is but one of many factors which lead to the conclusion that the rate is best left to the informed judgment of the Chancellor. The reason for this rule is explained by the Court of Appeals of New York in the opinion of Judge VANN cited above. On this further point Judge VANN says (p. 379):

> "If the funds in the hands of the court could have been distributed on the same day that the receiver was appointed, no claim of interest could have arisen, for there would have been no delay and no suspension of legal remedies. The delay in distribution, however, was the act of the law itself, and was essential for various purposes and among others to enable the creditors to prove their claims. 'As a general rule, after property of an insolvent passes into the hands of a receiver or of an assignee in insolvency, interest is not allowed on the claims against the funds.' (*Thomas* v. *Western Car Co.*, 149 U. S. 116.) Interest should not run in favor of one creditor at the expense of another, while the law, acting for all, is administering the assets. If the assets are sufficient to pay all, including interest, it must be paid, for as against the corporation itself interest should be allowed before the return of any surplus to the stockholders. As between the creditors themselves, however, no interest should be allowed during the process of administration, and the delay necessarily resulting therefrom, because the assets are equitably their assets, the administration is for their benefit and the delay is necessary to enable them to take action to present their claims in proper form, as well as to enable the court to put the assets in shape for distribution.
>
> "As the decree of dissolution relates back to the day when the court took possession of the assets, the delay is not the act or omission of the corporation, which is *civiliter mortuus*, but is owing to the law

and hence should operate neither to benefit nor prejudice any creditor. Distribution should be made as of the date when the delay began, for it was not only caused by the law but was necessary for the protection of all classes of creditors. As between the creditors themselves, therefore, interest ceases to accrue upon their respective claims, whether preferred or unpreferred, from the day when the corporation let go and the court took hold. This rule is so simple and easy of application that it will not only tend to prevent litigation, but will stimulate all creditors to frown upon delay and to promptly call the receiver to account. It will not induce preferred creditors to rest easy in reliance upon the expectation that they will make money through the misfortune of the corporation and, during the entire period of administration, receive interest at a greater rate than they had contracted for."

Reference should here be made to the decision on this question in *Board of Commissioners of Shawnee County, Kansas* v. *Hurley, et al.* (169 Fed. Rep. 92). The Opinion is written by Circuit Judge WALTER H. SANBORN and is liberally fortified by authorities. On points pertinent in the instant case Judge SANBORN says (p. 94):

"In the discussion of this question preferences, securities consisting of pledged or mortgaged property, such as are required to be surrendered or applied upon claims by the bankruptcy law, are laid out of consideration, and what is said has no reference to rights under them, because no such rights are in issue here. Laying out of view then such preferences and securities, the status of claims at the time of the filing of the petition in bankruptcy, and not at any subsequent time, fixes the rights of their owners to share in the distribution of the estate of the bankrupt. Bankr. Act. July, 1898, c. 541, Sec. 63a(1), 30 Stat. 562 (U. S. Comp. St. 1901, p. 3447); *Swarts* v. *Siegel*, 117 Fed. 13, 15, 54 C. C. A. 399, 401; *In re Bingham* (D. C.), 94 Fed. 796. On that date the property of the bankrupt passes from his control to the court or to its receiver, and thence

to the trustee in trust for the creditors of the bankrupt in proportion to the amounts of their claims at that time. On that date there vests in each creditor as a *cestui que trust* an equitable estate in such a part of the property of the bankrupt as the amount of his provable claim at that time bears to the entire amount of the provable claims against the estate. *On that date the bankruptcy law deprives the creditor of all his common-law remedies to collect his debt out of the property of his debtor and to collect subsequent interest on his claim against that property, and gives him in lieu thereof this equitable estate in the property of the bankrupt.* Thus the filing of a petition upon which a subsequent adjudication of bankruptcy is rendered places all the property of the bankrupt 'which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him' in *custodia legis.* Section 70a(5), 30 Stat. 566 (U. S. Comp. St. 1901, p. 3451). From that hour the bankrupt is divested of the power to appropriate it to the payment of his debts or to use and dispose of it at will, and that authority is vested in the District Court. Every suit against him upon a provable claim is stayed from the date of the filing of the petition. Section 11a, 30 Stat. 549 (U. S. Comp. St. 1901, p. 3426). Every person is forbidden to receive from the bankrupt any material amount of property after that date with intent to defeat the act. Section 29b, 30 Stat. 554 (U. S. Comp. St. 1901, p. 3433). Every intentional preference after that date is voidable. Section 60b, 30 Stat. 562 (U. S. Comp. St. 1901, p. 3445). Upon the filing of the petition the court may take immediate possession of the property if the bankrupt is neglecting it so that it is deteriorating in value. Section 69a, 30 Stat. 565 (U. S. Comp. St. 1901, p. 3450). And upon the appointment of the trustee all the property of the bankrupt 'which, prior to the filing of the petition, he could have transferred, or which could have been seized or sold under judicial process against him, passes to this officer of the court. Section 70a(5). Indeed, the condition at the time of the filing of the

petition measures the extent of the estate and the rights of all creditors of the bankrupt and all parties interested in the property throughout all the provisions of the law. Sections 1(10), 3b, 9b, 29(4), 68a(1), 30 Stat. 544, 546, 549, 554, 562 (U. S. Comp. St. 1901, pp. 3419, 3422, 3426, 3447)."

In proceedings under Section 77 there are certain new factors—first, the ultimate aim is reorganization rather than liquidation; and second, there has been introduced into proceedings under Section 77—perhaps in recognition of the complicated capital structures to which reorganization is to be applied—the use of different kinds and grades of securities designed to preserve creditor priorities as they existed at the inception of the proceeding.

The most that creditors could claim under Section 77 in preservation and protection of any lien priorities in respect of income *pendente lite* would be that each be given in the distribution of such income the same kind and grade of securities given him for principal of his claim at basic date. This would narrow the income problem down to the single question of the fair and equitable rate. In fixing the rate for the distribution of income among the different classes of creditors the Court gives consideration to many factors. In cases such as this one, which has been delayed many years by litigation between the senior creditors, a low rate should be indicated. Money rates current during the period of the delay should receive weight. Respect also should be accorded the views of the parties in interest who themselves should be the ones to propose a new Plan and fix the rate to be allowed on claims *pendente lite*. Here the dominant fact is that the property is theirs and the Court should give weight to their views as to what is equitable and just. In the present case the problem is simplified by the fortitous circumstance that income *pendente lite* is in excess of contract interest and 4% would be deemed a generous rate by creditors.

On facts of record as to which there is no dispute there would be no difficulty in formulating a Plan utilizing the Commission's basic valuation of $147,717,268 which would give due recognition to all creditors and stockholders and be compatible with the public interest.

Such a Plan would give recognition to all of the indebtedness of the Debtor as it existed November 1, 1935, in the amount as heretofore shown of $131,101,850—this being the aggregate of senior claims: $101,293,850 and the principal of the General Mortgage Bonds: $29,808,000. To this amount should be added income for ten years—from November 1, 1935 to November 1, 1945 measured by a fair percentage of principal which should not exceed 4%.* 4% would indicate an accretion of $52,440,740 as of November 1, 1945 and an allotment of new securities to creditors in the amount of $183,542,590 which would make all creditors whole and at the same time leave an equity for the stockholders in the amount of $16,615,418 without increasing the Commission's original basic valuation. The underlying principle of such a Plan would be that recognition up to $52,440,740 in new securities should be given for increased current assets and other accretions and for capital investments made by the Court.

The Debtor believes that such a Plan could be promptly negotiated with all creditors and put into effect without any delay unless head winds are met in the Interstate Commerce Commission. Added value due to economic changes between November 1, 1935 and November 1, 1945 far in excess of $52,440,740 could easily be justified—indeed an additional valuation substantially below that figure would indicate that much of the $43,000,000 spent on the property during trusteeship had been wasted.

* Income available for interest accrued to December 31, 1945 in the amount of $49,420,972 as shown by Annual Reports does not reflect heavy earnings of the Utah Fuel Company and various wholly owned subsidiaries; nor does it reflect income carried in reserves for which the necessity remains to be demonstrated.

In the formulation of the new Plan of Reorganization the rights of the Debtor, its junior creditors and stockholders in the capital stock of the Utah Fuel Company should be respected in the observance and not in the breach. Their rights are clear. The stock is pledged under the First Consolidated Mortgage of The Rio Grande Western Railway Company at a valuation of $6,000,000. The junior interests are entitled to withdraw their stock from pledge at this valuation or to have it sold at an upset price of $6,000,000 or (assuming but not admitting that appraisement is a constitutional substitute for a public sale for which the parties have expressly contracted) to have the stock separately valued in accordance with the law of the land which requires the independent judgment of a judicial tribunal upon both the law and the facts. Those of us whose admiration for the Interstate Commerce Commission is of the highest do not concede that it possesses expert qualifications for the appraisal of a coal operation in the State of Utah. The Plan should provide that any realization in excess of $6,000,000 be credited to the highest ranking junior creditor not made whole under its provisions and that this particular adjustment be made by payment in cash or in the most senior new security issued under the Plan. We think a public sale is the method less likely to involve constitutional infirmities and the one that should be pursued in view of the problems under the Commodities Clause of the Interstate Commerce Act which may arise if the Utah Fuel Company is not wholly divorced from carrier ownership (49 U. S. C. A. 1(8)).

Conclusion

In view of what is said in the Report of the Judiciary Committee and in the Opinions of Circuit Judges HUXMAN and PHILLIPS and of the newly informed judgment and judicial knowledge of this Court, it is respectfully submitted

that the proceeding should be referred back to the Interstate Commerce Commission in accordance with the direction of the Circuit Court of Appeals for the formulation of a new Plan as outlined above. The Opinions and Order of the Circuit Court of Appeals show a keen understanding that whatever the complicated scheme of Section 77 may be the Plan as made and the principles underlying its making need a plenary resurvey.

Respectfully submitted,

February 15, 1946.

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Appendix A

A Critical Analysis of Recent Reorganization Decisions of the Supreme Court of the United States†

FRANK C. NICODEMUS, JR.

In his dissenting Opinion in *Northern Securities Company* v. *United States*[1] the late Justice HOLMES has given us the oft-quoted epigram: "Great cases like hard cases make bad law." *Case, et al.* v. *Los Angeles Lumber Products Company, Ltd.*[2] was a hard case that has made bad law. The case was hard because first lien Bondholders having a valid debt of $3,807,071.88 secured by a prior lien on property having an appraised value of $830,000 were given new Preferred Stock for only $641,375—less than 25% of the full claim—under a Plan of Reorganization which allotted to junior interests (referred to as Class A Stockholders) a junior stock representing the balance of the appraised value of the mortgage estate.

The Plan had been approved and accepted by 92.81% of the first lien Bondholders and approved as fair and equitable by the District Court. The judgment of the District Court was affirmed by the Circuit Court of Appeals. The reorganization went on the rocks in the Supreme Court which condemned the Plan as unfair and inequitable because the first lien Bondholders were not given new securities for the full value of the property.

If that were the whole story; if the balance of the new securities representing $188,625 of the total value of the property had been given gratuitously to the junior interests the case would not make bad law. The District Court had found, however, that the allotment of a subordinate stock to the junior interests in the amount of $188,625 was supported by an adequate consideration. The Supreme Court

† This analysis was prepared for use of the Congress at the request of the Honorable HATTON W. SUMNERS, Chairman of the Judiciary Committee of the House of Representatives.

[1] 193 U. S. 197 (p. 400).

[2] 308 U. S. 106.

did not have before it the record that was before the District Court but nevertheless held that the considerations specified by the District Court, one of which was "continuity of management" constitute no legal justification for the issuance of the new stock to them. "Such items," the Court said, "are illustrative of a host of intangibles which if recognized as adequate consideration for issuance of stock to valueless junior interests would serve as easy evasions of the principle of full or absolute priority of *Northern Pacific Ry. Co.* v. *Boyd*[3] and relates cases." This determination pushes far too far the doctrine of these cases in none of which did any question of value arise and it applies to a reorganization the rigid rules applicable to a liquidation which it is the very purpose of a well conceived reorganization to avoid. Lien creditors ordinarily are investors whose objective is to remain in the enterprise as such and to assume no responsibility for management. To this end the lien creditor is permitted to make concessions in reorganizations to subordinate or equity interests which in a liquidation would be inadmissible. An examination of reorganizations over a period of fifty years will disclose hundreds of cases where lien creditors have accepted less than they would have received in liquidation in order to continue the enterprise and remain in it in an investor status. Income Bonds and Preferred Stock have been substituted for fixed interest bearing bonds frequently at lower interest or dividend rates and non-cumulative. Concessions such as these preserve for the investor the going concern value of the enterprise without changing his own status or requiring him to take over the burden of management and have heretofore been regarded as reasonable departures from the doctrine of strict priority. These factors motivated the first lien Bondholders of the *Los Angeles Lumber Products Company, Ltd.* in carving out of their own mortgage estate for the benefit of Class A Stockholders a new junior stock in the amount

[3] 228 U. S. 482.

of $188,625. They may have made a bad deal. The Supreme Court apparently thought they had made a bad deal, although the District Court had thought otherwise. The question, however, is one of business judgment and arises in an area where business judgment may lawfully be exercised and where a minority is protected by the self-interest of the majority.

Consolidated Rock Products Company v. *DuBois*[1] goes further than any previous case in its exploitation in reorganization of the doctrine of absolute priority. A Plan of Reorganization under Section 77B had been confirmed as fair and equitable by the District Court but on appeal was remanded by the Circuit Court of Appeals upon the sound and salutary ground that the Order or Decree of approval was not supported by detailed findings. In its Opinion, however, the Circuit Court of Appeals "made certain statements" which the Supreme Court thought did not "comport with the requirements of the absolute priority rule." The Supreme Court approved the reversal of the District Court but issued writs of *certiorari* "because of the importance in the administration of the reorganization provisions of the Act of certain principles enunciated by the Circuit Court of Appeals."

An analysis of the Opinion of the Supreme Court written by Mr. Justice DOUGLAS discloses three major propositions which the Supreme Court constructs upon the doctrine of absolute priority.

These are: (a) that a reorganization is unfair and inequitable which fails to treat interest on a parity with principal; (b) that a reorganization is unfair and inequitable which fails to accord "full compensatory treatment" to senior creditors who are asked to make sacrifices; and (c) that a reorganization is unfair and inequitable which gives recognition to junior interests unless supported by a valuation based upon "capitalization of prospective earnings."

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[1] 312 U. S. 510.

Each of these propositions which will be discussed briefly in its order is a departure from or an addition to the doctrine of strict or absolute priority as it has heretofore been applied in equity:

(a) *Interest:* The Plan of Reorganization which the Supreme Court condemned provided for the issue to senior lien creditors of Income Bonds and Preferred Stock (50% of each) for the full principal amount of their respective claims but made no provision for accrued interest which was extinguished under the Plan. The Supreme Court thought that this ran afoul of the absolute priority rule because "interest is entitled to the same priority as principal," referring as authority to the cases set out below.[5] These cases hold that the mortgage lien secures interest equally with principal and would fully sustain a ruling according interest parity of treatment with principal in a liquidation; but such treatment of interest is contrary to the established practice in equity reorganizations and to the finer traditions of our jurisprudence. What the Supreme Court has overlooked is that a contract for the payment of interest is different from almost every other contract known to the law. Since the dawn of history a contract for the payment of money for the use of money has been *sui generis*. Such a contract has always been subject to rigid governmental regulation and at times was completely outlawed by both the Jewish Church and the Christian Church. Under the Jewish Ecclesiastical Law up to the time of Rabbi Hillel forgiveness of a debt was mandatory after seven years and forgiveness of debt as a tenet of Christianity is uttered daily by millions in the Lord's Prayer. Interest problems perplexed the Athenians at the time of Solon nearly 600 years before the Christian Era. Later in Rome the subject was dealt with in the XII Tables which fixed a maximum rate of 8⅓%. But notwithstanding this Rome within a Century had become so debt ridden that the Government itself took over all

[5] *American Iron and Steel Mfg. Co.* v. *Seaboard Air Line Ry.*, 233 U. S. 261, 266, 267; *Ticonic National Bank* v. *Sprague*, 303 U. S. 406.

loans that were well secured and persuaded the holders of loans that were undercollateralized to accept lower interest rates and give to their unfortunate debtors the same kind of relief that was in the minds of Congress when it adopted Section 77 and Section 77B of the National Bankruptcy Act. In the Christian Era at the time of Marcus Aurelius the legal rate had risen to 12% and as the Emperor deemed this rate unconscionable he proceeded to drive the rate down by offering Government loans at 4%; and that is precisely what our own Government did in the early days of Reconstruction Finance Corporation. In England maximum rates were fixed from time to time by Parliament although there were periods in which Parliament, as did Solon, left the rate to be fixed by contract of the parties; but in the English Chancery Court the statutory rate was not binding. The Chancellor would not enforce a rate so far out of line with the prevailing commercial rate as to seem oppressive. Interest rates move up and down in response to the rise and fall of the National economy and thus it has been throughout history. It is not possible to fix an interest rate for a long period of years that will not become unfair before the time ends. Part of the time it will be too high, part of the time too low. It was the spirit of the common law as it came over to this Coun y from England that only contracts for reasonable interest were valid; and the laws and the literature of all civilized countries have encouraged leniency on the part of creditors. Yet the Supreme Court has apparently taken the position that it is unfair and inequitable for 66⅔% of a group of creditors to forgive all or any part of unearned or excessive contract interest due from a group of less fortunate debtors. The effect of the determination would seem clearly to be to overrule the Lord's Prayer and to issue posthumously to Shylock a patent of nobility. That the Supreme Court made its determination inadvertently and not deliberately may fairly be inferred from the circumstance that the Supreme Court

itself in the case of *Canada Southern Railway Company* v. *Gephard*[6] had approved as fair and equitable a Plan of Reorganization under which various Bondholders, some holding First Lien Bonds, others Second Lien Bonds, waived *all* interest and accepted in full settlement a new Bond at par for the principal of their debt.

(b) *Full Compensatory Treatment:* In the Opinion of the Supreme Court in *Northern Pacific Railway Company* v. *Boyd*[7] written by Mr. Justice LAMAR which has been referred to in the cases under review as the foundation of the doctrine of "absolute priority", there is the following statement:

> "This conclusion does not, as claimed, require the impossible and make it necessary to pay an unsecured creditor in cash as a condition of stockholders retaining an interest in the reorganized company. His interest can be preserved by the issuance, on equitable terms, of income bonds or Preferred Stock. If he declines a fair offer he is left to protect himself as any other creditor of a judgment debtor, and having refused to come into a just reorganization could not thereafter in a court of equity be heard to attack it."

This does not say or imply that the creditor "must be given full compensatory treatment and be made whole." The implication is precisely the reverse because there is but one method of measuring "full compensatory treatment" and that is by lawful money of the United States and this the Court expressly excludes. The traditional test of fairness is not the dollar measure but the preservation of the *priority* and this the Court says may be done by resort to an income bond or a Preferred Stock. To require that income bonds and Preferred Stock be issued in such quantity as to make the creditor whole is quite

[6] 109 U. S. 527.
[7] 228 U. S. 482.

obviously "to do the impossible." On the faith of an interpretation of *Northern Pacific Railway Company* v. *Boyd* which excluded the impossible there were many sound and successful reorganizations carried through in the earlier days in equity and more recently under Section 77B before the decisions of the Supreme Court in the cases under review. In many of these the senior lien creditor accepted an income bond or Preferred Stock for principal, waived interest for the depression period in which no interest was earned and left the equity undisturbed. In other cases the equity interests gave a part of their equity to the creditors or a Preferred Stock for unearned interest. There were a variety of Plans put through quickly that were satisfactory to all interests but which could not be sustained under the subsequent decisions of the Supreme Court. One of the last to get under the wire as will be seen from Moody's Industrial Manuals for 1937-1938 was the Baldwin Locomotive Works which contributed so much to our successful prosecution of the War and which is giving splended returns to the equity interests that would have been impoverished by a reorganization conforming to the subsequent decisions of the Supreme Court.

(c) *Capitalization of Prospective Earnings:* In *Smyth* v. *Ames*[8] the Supreme Court mentioned "the probable earning capacity of the property under particular rates prescribed by statute" as one of the many factors that might be considered in the ascertainment of the "fair value of the property" employed in the public service. This was not specified as a basic element but was relevant to the factor of "going concern value." If it had been regarded as a basic element of value its use would have created the "vicious circle" referred to in the dissenting Opinion in *Southwestern Telephone Co.* v. *Public Service Commission.*[9] The law of the land as to the ascertainment

[8] 169 U. S. 466.
[9] 262 U. S. 276.

of "the fair value" protected by due process was finally settled (or thought to be) by the Opinion of former Chief Justice HUGHES in the *Minnesota Rate Cases*.[10] Here the Supreme Court accepted reproduction cost less depreciation as the basic element of such a value but even this it did with the following reservation:

> "The cost-of-reproduction method is of service in ascertaining the present value of the plant when it is reasonably applied and when the cost of reproducing the property may be ascertained with a proper degree of certainty. But it does not justify the acceptance of results which depend upon mere conjecture."

The subject was reconsidered in the *Southwestern Telephone* case and in *St. Louis and O'Fallon Railroad Company* v. *United States*.[11] In these last mentioned cases Mr. Justice BRANDEIS sought to have the Supreme Court overrule *Smyth* v. *Ames* and substitute for the law of the land a new measure of value based upon prudent investment which he urged in two monumental dissenting opinions possesses the merit of certainty and stability said to be lacking in valuations under *Smyth* v. *Ames*. In neither of these opinions is it suggested that a valuation might be based upon capitalization of earnings; on the contrary the Justice objected to any consideration of regulated earnings as creating the "vicious circle." While it is true that factors other than reproduction new less depreciation may be considered as possible elements of value (certain of these are summarized in Note No. 6 to the dissenting opinion of Justices BRANDEIS and HOLMES in the *Southwestern Telephone* case) it is used as a basic, if not the basic factor, in all of the leading cases which involve confiscation to the extent that it may be ascertained with a proper degree of certainty and without conjecture.

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[10] 230 U. S. 352.
[11] 279 U. S. 461.

It may be here noted that there could be no mode of valuation resting more completely upon conjecture than capitalization of prospective earnings but since the decision of the Supreme Court in the case under analysis other methods are being discarded, although it would have been constitutionally bad for Congress to have prescribed such a method of valuation if it had tried to do so.[12]

The Railroad Reorganization Cases[13] referred to herein as the *Western Pacific* case and the *Milwaukee* case were argued together at the 1942 Term of the Supreme Court and were decided on March 15, 1943 under separate correlated Opinions, one by Mr. Justice REED rendered in the *Western Pacific* case, the other by Mr. Justice DOUGLAS rendered in the *Milwaukee* case. In each case the District Court had approved a Plan of Reorganization under Section 77 which the Circuit Court of Appeals reversed for lack of detailed findings deemed imperative under the ruling of the Supreme Court in *Consolidated Rock Products Co., Ltd.* v. *DuBois*. The Supreme Court granted *certiorari*. In the *Western Pacific* case it reinstated the Order of the District Court. In the *Milwaukee* case it reversed the Circuit Court of Appeals for requiring findings but allowed the case to be referred back to the Interstate Commerce Commission to reconsider the question whether the senior lien creditors who had insisted that the Plan accorded them full compensatory treatment had not dealt with themselves too ungenerously.[14]

The necessity for findings had been urged as being even more pressing in these cases than in *Consolidated Rock*

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[12] *Monongahela Navigation Co.* v. *U. S.*, 148 U. S. 312, and case cited under note 18.

[13] *Ecker, et al.* v. *Western Pacific Railroad Corporation*, 318 U. S. 448; *Group of Institutional Investors, et al.* v. *Chicago, Milwaukee, St. Paul and Pacific Railroad Company*, 318 U. S. 523.

[14] Afterwards there was an *opera bouffe* performance in the Interstate Commerce Commission where the senior creditors asserted that they had been "defeated" in the Supreme Court in their contention that they had been "made whole" and forthwith laid claim to some $15,000,000 of additional cash which the Interstate Commerce Commission graciously gave them.

Products Co., Ltd. v. *DuBois* for the reasons which the Supreme Court had assigned in that case.

The Supreme Court nevertheless held that while requirements for valuation are the same in a proceeding under Section 77 as in a reorganization under Section 77B it did not think there was anything in the *DuBois* case "to indicate that dollar valuations of the property or claims are essential for recapitalization or distribution of securities in reorganization." The fact that in the *Milwaukee* case the line of railway separately built and separately mortgaged and stretching from the Missouri River to Puget Sound was being taken without any valuation from the lienor and placed under a new mortgage in which the lienor was given no participation had not impressed the Supreme Court as having significance.

The opinions in these cases are fairly limited to questions presented by the record but it was obviously the intention of the Supreme Court that they should serve as a comprehensive guide to the Interstate Commerce Commission and the District Court in their future proceedings under Section 77.

Underlying both of these opinions is the proposition developed by the Supreme Court in its interpretation of Section 77 that Congress had intended to give the Interstate Commerce Commission the exclusive jurisdiction (1) to determine the value of a Debtor's property for the purpose of reorganization; (2) to determine the character and amount of reorganization capital; and (3) to determine the compatability of the reorganization with the public interest. These determinations the Supreme Court thought were to be final subject only to the limited judicial review which, in prior legislation Congress had prescribed for all determinations for the Interstate Commerce Commission. Mr. Justice ROBERTS and Mr. Justice FRANKFURTER dissented on the ground that a broader judicial review was necessary.

The Judiciary Committee of the House of Representatives in a formal official report has taken the position that the interpretation placed upon Section 77 by the Supreme Court as above summarized is contrary to the intent of Congress.[15] Since the Judiciary Committee speaks of actual knowledge it must be concluded as a fact that the Supreme Court was wrong; however justifiable its interpretation may seem in view of the complex provisions of Section 77.

This analysis is an effort to show why and where the Supreme Court went wrong and to suggest what may be done to quiet an aroused Congress and make Section 77 the useful and workable legislation which Congress had visualized.

The reason why the Supreme Court went wrong is that its approach to the problem of interpretation involved an apparent predisposition to give maximum power to the Interstate Commerce Commission and minimum power to the Court. Congress had not intended this if its intention is to be ascertained by the text of Section 77 construed in accordance with accepted canons of statutory construction.

The critical point where the Supreme Court went wrong was at the very beginning of Mr Justice Reed's opinion in *The Western Pacific* case which rejects the following constitutionally sound interpretation of Section 77 developed by the Circuit Court of Appeals:

> "In determining whether a plan of reorganization satisfies the requirements of subsection e, the court is not concluded by any determination made by the Commission, but may, and must, exercise its own independent judgment; and this is true whether such determination relates to value or to some other subject. Initially, however, the duty of determining the value of any property for any purpose under Section 77 rests on the Commission, not on the court. In re Western Pacific R. Co., 124 F. 2d, 136, 140."

[15] Report of the House Judiciary Committee on H. R. 4960, Seventy-Eighth Congress, Second Session, Report No. 1615.

Each of the three points where the Supreme Court held the Commission's jurisdiction to be exclusive to the extent indicated will be briefly analyzed under the captions (1) Valuation; (2) Capitalization; and (3) Public Interest, reserving for limited discussion at a subsequent point the question whether and to what extent appraisement is a valid substitute for public sale.

(1) *Valuation.* In the concluding paragraph of subsection (e) is the following provision for valuation:

> "If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

The interpretation of this very vital provision falls in two categories—first, the *finality* of the Commission's valuation thereunder; and second, the *method* of its valuation.

First, as to *finality*:—Referring to this category Mr. Justice REED in his opinion in the *Western Pacific* case notes that valuation is not specified in the first paragraph of subsection (e), as one of the subjects upon which the Court is required to make findings although it is also noted that a finding by the Commission that the equity or interest of a particular class of creditors or stockholders is without value is required by a subsequent paragraph of the same subsection to be affirmed by the Court. From the general

premise thus set up together with citations from the testimony in the Judiciary Committee of the House of Representatives Mr. Justice REED draws the following conclusions as to the finality of the Commission's action:

> "The power of the court does not extend to participation in all responsibilities of the Commission. Valuation is a function limited to the Commission, without the necessity of approval by the court. The first sentence of the last paragraph of subsection (e) provides:
>
> 'If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan.' The function of valuation thus left to the Commission is the determination of the worth of the property valued, whether stated in dollars, in securities or otherwise. One of the primary objects of the bill was the elimination of obstructive litigation on the issue of valuation and the form finally chosen approached as near to that position as seemed to the draftsmen legally possible. Judicial reexamination was not considered desirable. None of the findings required of the judge under subsection (e) relates specifically to valuation. Congress apparently intended to leave the determination of valuation 'of any property for any purpose under this section' to the Commission. The language chosen leaves to the Commission, we think, the determination of value without the necessity of a reexamination by the court, when that determination is reached with material evidence to support the conclusion and in accordance with legal standards. It leaves open the question of whether in reaching the result the Commission had applied improper statutory standards. This latter point is discussed under the heading of *Method of Valuation* in this opinion, p. 477, infra, where this plan is reviewed and upheld in this respect."

> "Assuming at this point that the Commission's valuation is sound and reached by allowable methods,

a matter discussed later in this opinion at page 477, we hold that the elimination of the claims of stockholders and creditors which are valueless from participation in the reorganization is in accordance with valid provisions of Section 77 (e). Actual bankruptcy means a loss to some investors. Subsection (e) recognizes this inevitable result and provides a method for their elimination from the reorganization proceedings."

"While by the terms of the statute the valuation of the property is left to the Commission, without participation by the court, this valuation must be made in accordance with the direction of the statute and as to that valuation is subject to judicial review. This review is limited in character by the direction of subsection (e) that valuation shall be determined by the Commission. The District Court may review to determine whether the Commission has followed the statutory mandates of subsection (e). Subsection (e) requires valuations by the Commission to be 'determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.' Thus, while judicial review does not involve an independent examination into valuation, it does require that the court shall be satisfied, upon the record before the Commission, with such additional evidence as may be pertinent to the objections to the Commission's finding of value, that the statutory requirements have been followed."

In reaching the conclusions set out above Mr. Justice REED appears to have given no weight to established canons of construction which if used would lead to a different conclusion from that which he reached. The Justice also

relied upon references to evidence before the Judiciary Committee which fall short of supporting the text of the Opinion.[15a]

A basic rule of construction asserting itself *in limine* and to which Mr. Justice REED gave no weight is the rule which requires a statute to be construed so as to avoid grave constitutional questions. Referring to this rule Chief Justice WHITE said:[16]

> "It is elementary when the constitutionality of a statute is assailed, if the statute be reasonably susceptible of two interpretations, by one of which it would be unconstitutional and by the other valid, it is our plain duty to adopt that construction which will save the statute from constitutional infirmity. *Knights Templars Indemnity Co.* v. *Jarman*, 187 U. S. 197, 205. And unless this rule be considered as meaning that our duty is to first decide that a statute is unconstitutional and then proceed to hold that such ruling was unnecessary because the statute is susceptible of a meaning, which causes it not to be repugnant to the Constitution, the rule plainly must

[15a] In support of the statement: "Judicial reexamination was not considered desirable" Justice REED refers to the hearings on H. R. 6249, pages 249-50; 291-92; 317. Much that is here said was in relation to the Commission's determinations of physical values under 19a and not over-all valuation under subsection (e). At pages 249-50 Chairman Sumners asked Mr. Fulbright (Railway Counsel) whether it could be constitutionally and practically arranged that the valuation in these proceedings be fixed by the Interstate Commerce Commission." Mr. Fulbright thought (with qualifying conditions) that it could; but he was afraid "that under this bill we would have to try the whole thing over again in the court and I do not think that ought to be done." So what Justice REED says may correctly reflect the state of mind of Mr. Fulbright but it manifestly does not state the view entertained by Chairman Sumners. At pages 291-292 the Chairman and a Committeeman (Mr. Robison) pursued the same inquiry. Following a series of questions directed to Mr. Marcus L. Bell, a member of the Committee of lawyers representing the Association of American Railroads, Mr. Robison finally asked: "Do you think we could write into the statute making the finding of fact—which is the finding of fact by the Commission—on valuation final?" to which Mr. Bell replied: "No, sir, I need only cite the O'Fallon case." At page 317 Mr. Leslie Craven speaking for Mr. Eastman says the final word: "I do not know that I understood Mr. Bell but t... have been views expressed here that you could delegate the valuation to the Commission for its final determination. That would perhaps be wise; I do not know that it would. But we doubt the constitutionality of it. We do not think you can submit to the Interstate Commerce Commission the final determination of that judicial issue."

[16] *United States* v. *Delaware & Hudson Co.*, 213 U. S., page 361, at 407-408.

> mean that where a statute is susceptible of two constructions, by one of which grave and doubtful constitutional questions arise and by the other of which such questions are avoided, our duty is to adopt the latter. *Harriman* v. *Interstate Com. Comm.*, 211 U. S. 407."

It must be assumed that the Judiciary Committee of the House of Representatives were conscious of this rule when they framed the concluding paragraph of subsection (e).

The first question therefore to be determined in reaching a sound construction of this paragraph is how far Congress can go within the limitations of the Constitution in giving finality to a valuation placed upon private property in a proceeding between private litigants not involving the eminent domain by an administrative board of laymen serving for limited terms under executive appointment confirmed by the Senate.

The answer to this question which may be given readily and categorically is different from that given by the Supreme Court in the decisions under analysis. The correct answer is:

Congress may give such a board jurisdiction to fix such a valuation with finality and without judicial review only when its use does not involve the taking of private property.

Ordinarily this allows finality and excludes judicial review of any valuation under subsection (e) which is high enough to provide full participation for all creditors and stockholders. This is a reason, if not the reason, why the Judiciary Committee of the House did not specify valuation as one of the factors to be dealt with in the findings of the Court. The taking of private property is not involved where recognition is given in reorganization to all creditors and stockholders and this, it may be added, is the kind of a reorganization which Congress had in mind

when it enacted Section 77 and Section 77B and later the Chandler Act—all "for the relief of debtors."[17] In such a case valuation becomes a mere abstraction with which the Court is not concerned; all that the Court does in such a case is to satisfy the judicial conscience that all parties in interest are participating; that each participant has been dealt with fairly and equitably; and that his priority, if any, has been respected.

The great constitutional question to which scant if any consideration is given in the opinions of Justices REED and DOUGLAS arises when the Commission's over-all valuation (which contrary to the expectations of Congress it invariably is) is too low to provide such participation for junior creditors or equity interests. Here the constitutional limitation comes into play to deprive the Commission's valuation of every shred of finality and to put upon the Court an imperative judicial duty to disapprove the Plan unless "satisfied"—a word of too definite import to admit of judicial surgery—that the Plan "conforms to the law of the land regarding the participation of the various classes

[17] One of the very ancient canons of statutory construction is that the preamble and declared policy of the statute are an almost infallible guide to the intent of the legislature. In the recent third Edition of Sutherland on Statutory Construction in Section 4804 we find the rule stated in the following language:

> "The key to the opening of every law, is the reason and spirit of the law * * * it is to the preamble more especially that we look for the reason, or spirit of every statute; rehearsing * * * as it ordinarily does, * * * in the best and most satisfactory manner, the object or intention of the legislature."

Turning to the caption of Chapter VIII of the Bankruptcy Act of which Section 77 forms a part it will be found to be entitled "Provision for the Relief of Debtors." But Congress was not content to have the reason and spirit of this legislation shown only by the title or preamble. Congress went further and in Section 73 it expressly repeated and declared what was said in the title or preamble to be the Congressional policy applicable to Sections 74, 75 and 77. So it was made perfectly clear that Congress intended that Section 77 should be administered and applied as a relief statute and should not be used by the Interstate Commerce Commission to destroy and wipe out the property rights of the very persons for whose benefit it was passed. It is interesting to note that this preamble and Congressional declaration of policy was called to the attention of the Supreme Court in oral argument and in at least four different Briefs filed in the *Western Pacific* case and the *Chicago, Milwaukee* case but is nowhere mentioned either in the opinion of Mr. Justice REED in the *Western Pacific* case or in the opinion of Mr. Justice DOUGLAS in the *Milwaukee* case.

of creditors and stockholders." The statute does not say that the Court must be satisfied if "the statutory standards for valuation have been followed" or that the Court must be satisfied if "it finds no legal objection to the Commission's use of its own valuation"—what it does say is that the Court must be satisfied that the Plan is fair and equitable and "conforms to the law of the land regarding the participation of the various classes of creditors and stockholders," and the law of the land is clear, definite and specific that no creditor or stockholder may be deprived of his property even in a proceeding for eminent domain by a valuation that is not *wholly* judicial.

The cases set out below are the classic authority for the fundamental constitutional proposition—one that strikes at the root of the cases under analysis—that valuation for the purpose of divesting the owner of private property is exclusively judicial.[18]

In the case last cited in an opinion written by former Chief Justice HUGHES the rule is thus epitomized:

> "The case of confiscation is illustrative, the ultimate conclusion almost invariably depending upon the decisions of questions of fact. This Court has held the owner to be entitled to 'a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both law and facts.'"

Congress knew that under a line of decisions of the Supreme Court judicial review of administrative orders had ceased to have any practical value; it knew that the Interstate Commerce Commission had learned the art of rendering innocuous the limited judicial review of its valua-

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[18] *Monongahela Navigation Co.* v. *United States*, 148 U. S. 312; *Ohio Valley Water Company* v. *Ben Avon*, 253 U. S. 287; *St. Joseph Stockyards Company* v. *United States*, 298 U. S. 38; *Baltimore & Ohio Railroad Company* v. *United States*, 298 U. S. 349; *Ohio Bell Telephone Company* v. *Public Utilities Commission*, 301 U. S. 292; *Cleveland Railway Company* v. *Backus*, 164 U. S. 439; *United States* v. *Boston and New York Canal Company*, 271 Fed. 877; *Crowell* v. *Benson*, 285 U. S. 22.

tion orders permissible under existing statutes and decisions of the Supreme Court. The process had been explained in the dissenting opinions of Justices BRANDEIS and HOLMES in the *Southwestern Telephone* case.[19] Here the Justices say of the rule of *Smyth* v. *Ames*:

> "The efforts of courts to control commissions' findings of value have largely failed. The reason lies in the character of the rule declared in *Smyth* v. *Ames*. * * * The result, inherent in the rule itself, is arbitrary action, on the part of the rate regulating body. *For the rule not only fails to furnish any applicable standard of judgment, but directs consideration of so many elements, that almost any result may be justified.*"

The Judiciary Committee of the House which, with the aid of counsel for the Federal Coordinator of Transportation, framed subsection (e) of Section 77 did not care to commit to the Interstate Commerce Commission even if it had constitutional power to do so (which it lacked) a jurisdiction to order the taking or forfeiting of private property on the basis of a valuation which was subject only to a judicial review that had been condemned as useless by Justices HOLMES and BRANDEIS. Had the Committee desired a review of that character all they needed to do was to remain silent; it already was provided by the existing law. They aimed, however, for something both useful and Constitutional and accordingly gave to the Court a mandate to review every factor that entered into a reorganization before giving it judicial approval and expressly enjoin judicial disapproval unless the Court is satisfied on every vital point. In any reorganization that excluded from participation all or any part of a class the Court was required by Clauses (1) to (3) of the first paragraph of subsection (e) to be satisfied upon every factor affecting the fairness and propriety of the reorganization which includes necessarily

[19] *Southwestern Telephone Co.* v. *Public Service Commission*, 262 U. S. at pp. 296-298.

and inevitably—Valuation, Capitalization and Public Interest. These three factors will be separately considered at a subsequent point. It may here be noted, however, that in the opinions of both Justices REED and DOUGLAS considerations of capitalization and public interest were apparently deemed to be factors having some bearing upon valuation—a concept which finds no support in the law of the land.

The possibility that the Interstate Commerce Commission might attempt to justify a confiscatory reorganization on some notion of public interest had not been overlooked by counsel for the Association of American Railroads and they filed with the Judiciary Committee of the House of Representatives which was considering recommendations of the federal Coordinator of Transportation (the Hon. Joseph B. Eastman) an objection to the language of the proposed valuation clause of subsection (e). Mr. Eastman appeared before the Judiciary Committee in advocacy of the amendatory legislation and said in opening:

> "I shall not speak at length this morning, gentlemen, because I want most of the talking to be done by my counsel, Mr. Leslie Craven, who has made an intensive study of this matter and is much better equipped to deal with the details than I am. Commissioner Mahaffie of the Interstate Commerce Commission is also here and he is exceedingly well informed in regard to railroad financial matters having dealt with them for many years, first as director of the Bureau of Finance of the Commission and afterward a Commissioner, a member of Division 4 of the Commission which deals with financial matters" (p. 13).

Mr. Craven and Mr. Mahaffie were thus accredited by Mr. Eastman to speak for him as the sponsor of the legislation. Later in the hearing Mr. Craven with Mr. Mahaffie standing by made the following answer to the suggestion of counsel for the Railroads that the Commission might attempt to coerce reorganization on the basis of depression earnings:

> "Of course that makes a perfectly outrageous picture and there is not anybody in his sane mind who would propose that these railroads be reorganized now on any such basis. Nobody proposes that. You could not get any such thing as that through a court to save your life" (p. 325).[20]

This was a representation made to the Judiciary Committee by the duly accredited representative of Mr. Eastman—a representation accepted without reservation or objection by Mr. Mahaffie—that Section 77 would not and could not be construed by the Interstate Commerce Commission as authorizing the Interstate Commerce Commission to do what it has done in these railroad reorganization cases and which the Supreme Court appears to have sanctioned.

Second, as to *Method*: This category of the valuation problem under Section 77 divides naturally into two subcategories: (a) a critical study of the past; and (b) a constructive program for the future.

In the two principal cases under analysis, the *Western Pacific* case and the *Milwaukee* case and the companion proceeding for the reorganization of the *Chicago and North Western Railway Company*, in which *certiorari* was denied, valuable equities were forfeited on the basis of a valuation by prophesy. The factor upon which the prophesy was based was depression earnings. While in all three cases the Interstate Commerce Commission made prolific references to other factors which embraced all of those set out in note 6 to the Opinion of Justices BRANDEIS and HOLMES in the *Southwestern Bell Telephone* case there was no factor that would not discredit the prophesy except depression earnings.

In the *Western Pacific* case the Commission found a capitalizable value of $85,013,472 although it was undis-

[20] Hearings before Judiciary Committee on H. R. 6249, Seventy-fourth Congress, First Session, pp. 13, 325.

puted that depreciated cost as of December 31, 1938 was in excess of $120,000,000 and the 19-A valuation was in excess of $150,000,000. An allowance of $120,000,000 would have fully protected the junior debt and capital stock. There had been periods of low and high earnings but measures to stabilize earning power at a high level were halted temporarily by the depression; part of the junior debt and the entire capital stock were forfeited on a valuation having no substantial factual support except depression earnings.[21]

In the *Milwaukee* case the Commission found a capitalizable value of $548,533,312, although the Commission filed a Report of its Bureau of Valuation showing that cost of reproduction new less depreciation plus the value of lands and rights and a stated amount of working capital amounted as of December 31, 1935 to $653,007,696. More than $100,000,000 of invested capital upon which there had been substantial earnings right up to the depression was extinguished as valueless by the Commission. There was no finding as to earning power except the negative one that "there is no evidence whatever to indicate that a recovery of the earning power of 1928-9 is reasonably probable."[22]

The case of *Chicago and North Western Railway Company* is one of the most tragic that could well be imagined and one of the most indefensible. This Railroad Company's total capitalization as of December 31, 1931, including interest accruals to that date, amounted to $612,253,200. The cost of reproduction new less depreciation plus the value of lands and working capital for the system properties was found by the Commission to be $676,793,588. $180,835,200 of the total capitalization was represented by Preferred and Common Stocks upon which dividends had been earned and paid as shown by the following table:

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[21] Brief of Debtor, Nos. 7, 8, 20, 33 and 61, October Term, 1942, pp. 26-27.
[22] Brief of Debtor, Nos. 11-19, 32, October Term, 1942, p. 19.

	Com.	Pfd.		Com.	Pfd.
1864....	..	3½%	1901....	6%	7%
1865....	..	3½%	1902....	7%	8%
1868....	5%	5%	1903....	7%	8%
1869....	9%	12%	1904....	7%	8%
1871....	10%	10%	1905....	7%	8%
1872....	3½%	7%	1906....	7%	8%
1873....	..	7%	1907....	7%	8%
1876....	..	2½%	1908....	7%	8%
1878....	3%	7%	1909....	7%	8%
1879....	4%	7%	1910....	7%	8%
1880....	6%	7%	1911....	7%	8%
1881....	6%	7%	1912....	7%	8%
1882....	6½%	7¼%	1913....	7%	8%
1883....	7%	8%	1914....	7%	8%
1884....	7%	8%	1915....	7%	8%
1885....	7%	8%	1916....	7%	8%
1886....	6%	7%	1917....	7%	8%
1887....	6%	7%	1918....	7%	8%
1888....	6%	7%	1919....	7%	8%
1889....	6%	7%	1920....	6%	7%
1890....	6%	7%	1921....	5%	7%
1891....	6%	7%	1922....	5%	7%
1892....	6%	7%	1923....	5%	7%
1893....	6%	7%	1924....	3½%	7%
1894....	6%	7%	1925....	4%	7%
1895....	7%	7%	1926....	4%	7%
1896....	5%	7%	1927....	4%	7%
1897....	5%	7%	1928....	4½%	7%
1898....	5%	7%	1929....	4½%	7%
1899....	5%	7%	1930....	4%	7%
1900....	6%	7%	1931 (to June 30)	2%	3½%[23]

The Preferred and Common Stock with the above indicated earnings record running up and in to the depression which is perhaps the most impressive record of any Railroad Company if not any corporation in the financial history

[23] Petition for *certiorari* Nos. 999-100-101; Chicago & North Western Railway Company Reorganization, 236 I. C. C. 575, 579; Poor's Manual of Railroads, 1931, p. 661.

of the United States was declared worthless by the Interstate Commerce Commission. The only factor to which any weight could have been given in such an appraisal was *depression* earnings.

There is a constitutional question whether ownership of private property may be forfeited or extinguished in a proceeding of this nature on the basis of a mere appraisal. The mortgage creditor ordinarily contracts to give to his debtor a public sale and this contract is private property of the debtor protected by due process. Similar protection is afforded to debtors generally by the local law of most states. To substitute for the protection of a public sale an appraisal resting in a large measure upon conjecture or upon what the late Joseph B. Eastman described as "an educated guess" is to raise a question of grave constitutional import. This question had not arisen and was not considered in *In re 620 Church Street Corporation*,[24] referred to by Mr. Justice REED to support his statement "the present plan may not be successfully attacked on the ground that Congress is powerless to authorize in bankruptcy the elimination of claims without value." In this case there had been judicial appraisal which the parties did not contest and as to which there was apparent agreement. It is not authority for the elimination of an equity as having no value because it is said to be without value by an administrative Board and is not authority for the rejection of a demand for a public sale by a party in interest who seeks it as a protection against the devaluation of his property. Provision for such a sale is made as a constitutional safeguard in both Section 77 and Section 77B but never has been utilized.

Assuming, however, for purpose of discussion that appraisement is a constitutional substitute for a public sale in proceedings under Section 77 the three railroad reorganizations referred to above may fairly be criticized as constitutionally unsound because (a) they permit private rights

[24] 299 U. S. 24.

to be forfeited and titles divested on the basis of an appraisement or valuation which is administrative and non-judicial whereas to be valid for such purpose and use it must be wholly judicial; and (b) they tolerate the exclusive use in such an appraisement or valuation of a factor not heretofore recognized by the law of the land: *prophesy.*

Mr. Justice DOUGLAS says in his opinion: "Certainly there is no constitutional reason why earning power may not be used as the criterion for determining value for reorganization purposes and it is our view that Congress when it passed Section 77 made earning power the primary criterion." There *is* a definite constitutional reason. The law of the land does not include earning power which is not susceptible of proof as the primary factor in a valuation to be used in confiscating private property. Expropriation on such a basis is necessarily arbitrary and in violation of due process. The use of such a factor makes possible the shocking results shown in the Report of the Judiciary Committee of the House of Representatives to which reference was heretofore made. Congress itself in subsection (e) expressly qualified the use of the earnings factor by the requirements of the law of the land.

A constructive program for the future which will avoid the tragic errors of the past as reflected by or revealed in these three railroad reorganizations may properly be asked as a justification for the criticism levelled against them. It may be admitted that criticism to be effective should be constructive and in the language of the common law should "give a better writ."

Ever since *Smyth* v. *Ames* the valuation of railroads and utilities has been a subject presenting many difficulties. There is a wealth of learning or discussion but no fixed or definite rule. The subject is complicated but not clarified by an idea featured in the opinion of Mr. Justice DOUGLAS "that value is a word of many meanings." This statement credited to Mr. Justice BRANDEIS is merely the expression

of an irrelevant truth. Whenever an appraisement or valuation is made to be used to deprive an owner of his property there is but *one* value and that is the value protected by the Fifth Amendment. The constitutionally protected value may not be undermined and written down by calling it "reorganization value" or by giving it some other name equally uninformative and inadmissible.

As the result of trial and error over the long period that has elapsed since *Smyth* v. *Ames* reproduction new less depreciation has emerged as the most dependable basic factor or criterion of value for the great majority of cases. There are cases where it is of little or no dependability but these are the exception and not the rule. The recent case of *Market Street Railway Company* v. *Railroad Commission of California*[25] is a fair illustration of the exception. Here a transit system had lost its economic value through obsolescence. The earlier case of *Atlanta, Birmingham and Coast Railroad Company* v. *United States*[26] is an equally good illustration. Here a railroad constructed primarily as a lumber road into an otherwise unproductive area ceased to have economic value when the lumber was exhausted. Reproduction values of these properties were deemed of no significance but this conclusion was based upon existing provable facts. In the absence of such provable facts reproduction costs equated to current prices represents the constitutionally protected value (subject to actual depreciation) of the debtor's property for the determination of the existence or non-existence of an equity for junior creditors and capital stock.

(2) *Capitalization.* Much is said in the opinions of Mr. Justice REED and Mr. Justice DOUGLAS on the subject of capitalization and the term is used almost as a synonym for valuation. In fact Justice REED expressly says:

> "* * * we are of the opinion that the determination by the Commission of the aggregate amount of

[25] 324 U. S. 548.
[26] 296 U. S. 33.

> securities which may be issued against the system is in substance a finding of total value for reorganization."

Earlier in the opinion the Justice had also said:

> "The development of the capitalization of the reorganized Company which is entrusted solely to the Commission under the requirement that the plan be compatible with the public interest is that relating to the total amount of issuable securities and the quality of the securities to be issued."

Little is said in Section 77 of this subject. Specific authority is given by subsection (b) to the Interstate Commerce Commission to limit the proportion of the total authorized capitalization which is to be represented by fixed interest bearing debt but no attempt was made to deal with other phases of capitalization. The fact that Congress did deal specifically with one phase of capitalization excludes under familiar rules of interpretation an implied grant of a broader power which would include that with which it dealt with specifically.

Since the passage of the Transportation Act, 1920, regulatory power over the issue of securities of interstate rail carriers has been vested in the Interstate Commerce Commission under Section 20-A of the Interstate Commerce Act. This express statutory power must be as broad as the implied power which the Supreme Court built up upon the requirement that the plan be compatible with the public interest because this identical requirement is a part of the same Section 20-A. It is therefore not clear and may not be of significance why the Supreme Court thought it necessary or expedient to spell out of the reference to the public interest in subsection (d) a grant of power to limit and control capitalization.

The opinions in both of the two cases under analysis are silent on the basic constitutional issue which Section 77 as construed by the Supreme Court so clearly presents—

the power of Congress to authorize an administrative Board by *fiat* to take or forfeit title to private property protected by due process. This is an issue that cannot be avoided. It is of course immaterial how the expropriation or forfeiture is to be achieved—whether by under-valuation or by under-capitalization. Confiscation is a thing of substance not of terminology. Protection against it is guaranteed by the Constitution through the untrammelled exercise of the judicial power vested in the Courts. Congress could not lawfully transfer that high function to an administrative Board such as the Interstate Commerce Commission and under Section 77, properly construed, it has not tried.

It is true that Mr. Justice REED has also said:

> "While the public interest phase of capitalization is not to be independently passed upon by the Court the Court does have statutory authority to review for obedience to legal standards."

This understates and unduly limits the essential judicial review of the Commission action in two aspects: it misinterprets and interprets unconstitutionally the pertinent provisions of subsection (e) of Section 77.

Subsection (e) is an unconditioned mandate from Congress to the Courts to disapprove any Plan certified to any of them by the Interstate Commerce Commission unless the Court is satisfied, among other things, that the Plan is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders and conforms to the law of the land regarding participation of various classes of creditors and stockholders. Obedience to this mandate on the part of the Court is not excused by the failure or refusal of the Interstate Commerce Commission to authorize a new capital structure that will provide recognition and participation for a class or classes whose property is being confiscated. The language of subsection (e) and of Section 77 as a whole admits of no such emasculating qualification.

Under the plain unambiguous language of subsection (e) and under the law of the land which Congress has no power to alter the injured class has an absolute right to go to the Court and demand that the Court give that class a square deal, not upon the basis of what an administrative Board has done or said but "upon its own independent judgment as to both law and facts."

(3) *Public Interest.* In a capitalistic economy it is difficult to understand why and how the confiscation of private property should or could be in the public interest. In a privately owned and operated industry such as the great system of American railways it is equally difficult to understand why and how the credit of that industry will be enhanced by the confiscation of a substantial part of the equity capital already invested therein. The fact that these questions reflect what appears to be the current philosophy of the Interstate Commerce Commission to which Congress has granted almost unlimited regulatory power over the $25,000,000,000 railway industry may be adequate cause for alarm among those whose capital is invested in railway securities but is not an aid in the analysis of the Supreme Court decisions which fail to excoriate that philosophy.

It is clear that a lower invested capital will permit a lower rate base and that a lower rate base will be a step forward toward lower cost transportation. There may be, although the point is debatable, a public interest in low cost transportation but that is not a justification for depressing the value of railway properties. The lowering of railway valuations for the purpose of securing low cost transportation is a very direct violation of the inhibition against the taking of private property for public use without just compensation and as such should be condemned by the Courts. No strength is added to the determination of the administrative Board by attributing what it does in forfeiting equities to the public interest or to an authority over capitalization and by integrating as do Justices REED

and DOUGLAS in the cases under analysis the three factors of valuation, capitalization and public interest. When the forfeiture of private property is involved the inhibitions of the Constitution apply with equal force as limitations upon the exercise by a non-judicial body of each of these separately stated powers.

Incidentally it should be noted that in inserting in subsection (e) a specific requirement that the Commission must find every approved Plan to be compatible with the public interest it was not done in any relation to capitalization. This was already provided for by Section 20-A of the Interstate Commerce Act in identical language brought into Section 77 by subsection (f).

The foregoing covers what are conceived to be those major errors in the recent reorganization decisions of the Supreme Court which might be dealt with correctively either by Congress or by the Court itself. There are others which although less fundamental seem of sufficient consequence to be noted and briefly discussed.

A very serious invasion of vested property rights of junior interests and a departure from what seems to be the apparent intent of Congress as declared in subsection (l) of Section 77 is resulting from the determination of of the Supreme Court that the Interstate Commerce Commission is given plenary power by subsection (b) to move backward and forward the effective date of a Plan of Reorganization. The Interstate Commerce Commission is exercising this power without interference by the Courts regardless of its reaction upon vested property rights, particularly those growing out of the lawful impounding by lienors of income earned *pendente lite*. In the *Milwaukee* case it appeared that a substantial if not the larger part of income earned during trusteeship and amounting to over $100,000,000 had been earned on lines between the

Missouri River and Puget Sound. The lien of the First Mortgage resting upon this extensive property had been displaced by the Plan on the theory (but without lawful evidence) that it lacked earning power and the prior right of the lienor to the income earned *pendente lite* was subordinated to claims of more favored groups of creditors. The Circuit Court of Appeals thought it "perhaps pertinent to note that Section 77(l) rather plainly provides that the date of filing of the Debtor's petition shall be the effective date of the Plan" but that Court felt bound by the decision of the Supreme Court rather than by the statute. The Supreme Court denied *certiorari.*[27] It is doubtful whether the Supreme Court understood all the implications of this determination and on further consideration may limit its effect.

Subsection (e) is quite explicit that if the Court shall disapprove a Plan there shall be a reference back to the Commission for further action and that the Commission shall proceed to a reconsideration of the proceeding under subsection (d). The last named subsection provides for the filing by a debtor or 10% of any class of creditors or stockholders of a Plan. The obvious construction of the two subsections, (e) and (d), taken together is that upon a reference back when a Plan has been disapproved the debtor or 10% of any class of creditors or stockholders shall file within the statutory period a new Plan.

In the *Milwaukee* case and perhaps others the Courts and the Interstate Commerce Commission have assumed the power to exclude from the proceeding any party whose interest has been declared to be without value. In the *Milwaukee* case the Interstate Commerce Commission denied the Debtor the right to file a new Plan or to have a further hearing or introduce additional evidence designed to establish a right to participation not accorded under

[27] *In re Chicago, Milwaukee, St. Paul and Pacific Railroad Company,* 145 Fed. Rep. 2nd 299; 324 U. S. 857.

the defunct Plan. Nevertheless the Commission itself formulated a new Plan. The Debtor undertook to show but was denied the right to show that between the date of the certification of the disapproved Plan and the reference back from the Court to the Commission there had been tremendous accretions to the trust estate which had established value for the capital stock. The Debtor's petition was an impressive one. It alleged:

> "It was in 1940 on the basis of a record closed on March 22, 1938, that the Commission limited the total capitalization of the reorganized Debtor to $548,533,321 and found that the equity of the existing stockholders was without value. Since then the Debtor's cash balance has increased by about $112,000,000, a sum greater than the entire amount of fixed interest bearing obligations authorized in the Plan then approved. If the capitalizable value of the Debtor's property was then equivalent to $548,533,321 of securities then authorized it must now by reason of this increased cash be $112,000,000 greater. Such an amount cannot be ignored in determining value for capitalization or any other purpose. These changes are accomplished facts. They do not rest on hopes for the future or prospective earnings. The cash is in the till. Efficiency has been increased. The remote possibility of earning power greater than in the previous period has become an actuality."

The Interstate Commerce Commission denied the petition on the ground that everything was foreclosed by the Supreme Court except those matters which it had expressly disapproved or questioned. The exclusion of the Debtor from further participating in the proceeding is contrary to the apparent intent of Congress and runs counter to the established rule that equity speaks as of the date of its own final decree.[28]

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[28] *Randel* v. *Brown*, 2 Howard 406, 423; *United Corporation* v. *Federal Trade Commission*, 110 Fed. (2d) 473; *Stonega Coke and Coal Co.* v. *Price*, 106 Fed. (2d) 411, 419.

It was never intended by Congress that Section 77 was to be utilized as a streamlined foreclosure—a proceeding to facilitate the forfeitures which equity has traditionally abhored. On the contrary Section 77 was conceived as a remedial statute, one that was to be permissive and not coercive under which 66⅔% of the creditors and stockholders were to have the privilege without the delay and expense of foreclosure of agreeing upon a capital readjustment of the kind described in subsection (e). This was a privilege of which they could avail or not as they saw fit. The preexisting equity procedure was left open as an alternative by subsection (i).[29] It was assumed that in most cases the bankruptcy procedure would be preferred but if a Plan was not carried through expeditiously the proceeding was to be dismissed and the parties left to their existing remedies at law and in equity. A different interpretation has diverted Section 77 from its true purpose and as a result the legislation has become thoroughly discredited. The administration of justice under its provisions is at a low ebb. In the words of Falstaff who made comedy out of tragedy: "* * * there is no equity stirring."

February 2, 1946.

[29] The recent case of *New England Coal and Coke Company* v. *Rutland Railroad Company*, 143 Fed. Rep. 2nd 179, is as yet hardly an authority to the contrary. The nature of the Court's opinion is sufficiently revealed by the following excerpt: "As several Supreme Court Justices and commentators have said, some judicial legislation is one of the unavoidable facts of life."

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1945.

Nos. 278-282.

RECONSTRUCTION FINANCE CORPORATION and Others,
Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY and Others,
Respondents.

BRIEF OF GUY A. THOMPSON, TRUSTEE, MISSOURI PACIFIC RAILROAD COMPANY, DEBTOR.

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Respondents.

BRIEF OF GUY A. THOMPSON, TRUSTEE, MISSOURI PACIFIC RAILROAD COMPANY, DEBTOR.

STATEMENT.

This proceeding comes to this Court on writs of certiorari to review a Decree of the United States Circuit Court of Appeals for the Tenth Circuit, dated May 10, 1945, which reversed two separate Orders of the District Court for the District of Colorado; one an Order dated October 25, 1943, approving a Plan of Reorganization for

the Respondent, The Denver and Rio Grande Western Railroad Company under Section 77 of the National Bankruptcy Act* (hereinafter referred to as Section 77), the other an Order dated November 29, 1944, confirming the same Plan of Reorganization after its rejection by the requisite percentage of the Debtor's General Mortgage Bonds.

This Respondent (hereinafter for brevity referred to as Missouri Pacific Trustee) desiring a reconsideration of the decisions of this Court rendered March 15, 1943, in the **Western Pacific** and **Milwaukee** cases** filed his petition for a writ of certiorari which has not as yet been acted upon by this Court (No. 291, October Term, 1945).

QUESTIONS PRESENTED.

The specific question presented is: Does the Plan of Reorganization as confirmed by the District Court make adequate provision for a fair and equitable treatment for the interests and claims of the Debtor's General Mortgage Bonds, and was the rejection of the Plan by the General Mortgage Bondholders reasonably justified in light of their respective rights and interests and all the relevant facts?

POSITION OF MISSOURI PACIFIC TRUSTEE.

The Missouri Pacific Trustee (R. 655†) holds title to 150,000 (50%) of the outstanding shares of the no-par common stock; $608,000 par value of the outstanding preferred stock; and $1,000,000 of Refunding and Improve-

* 11 U. S. C., Sec. 205.

** Ecker et al. v. Western Pacific Railroad Corporation, 318 U. S. 448; Group of Institutional Investors et al. v. Chicago, Milwaukee, St. Paul and Pacific Railroad Company, 318 U. S. 523.

† Refers to page of printed record.

ment Mortgage Bonds of The Denver and Rio Grande Western Railroad Company (sometimes referred to herein as the "debtor"); and because of such ownership, the interests of Missouri Pacific Trustee will be materially and adversely affected if the Plan should finally be put into effect by reason of the fact that the Plan certified to the Court contains a finding by the Commission that the equities of the owners of the common and preferred stock of the Debtor have no value, which finding was confirmed by the District Court and also by the United States Circuit Court of Appeals for the Tenth Circuit. The opinion of the Circuit Court of Appeals (R. 254) contains the following:

> "Nothing in this opinion shall prejudice or foreclose the rights of the parties to propose a new plan of reorganization or the power of the Commission to formulate, approve, and certify a new plan of reorganization in the light of any relevant facts presented to the Commission in any proceeding under 11 U. S. C., Sec. 205 (d)."

If, therefore, the Order and Decree of the United States Circuit Court of Appeals for the Tenth Circuit requiring this cause to be referred back to the Commission stands, the Missouri Pacific Trustee will be in a position to again try out before the Commission the question of whether the common and preferred stock in the Debtor is of value. The Missouri Pacific Trustee filed with this Court his petition for certiorari (No. 291) to review the Order or Decree of the United States Circuit Court of Appeals for the Tenth Circuit because, in the opinion of that Court, it was stated that the equities of the common and preferred stockholders of the Debtor were without value and Missouri Pacific Trustee was unwilling to permit that view of the said Court of Appeals to remain uncontested, it being the contention of such Trustee that having regard to the

value of the properties of the Debtor and the changed economic conditions surrounding the operation of that property, together with a proper method of valuation, the equities of the common and preferred stockholders were not without value and that the Commission, the District Court and the Circuit Court of Appeals should have so held.

Inasmuch as the petition of Missouri Pacific Trustee for a writ of certiorari directed to the Circuit Court of Appeals has not been acted upon, it is assumed that the Court in this proceeding will deal only with the issues raised in the petition for certiorari (Nos. 278-282) filed by the Senior Bondholders.

We shall, however, briefly call to the attention of the Court certain changed conditions which in our view not only show that the claims of the General Mortgage Bondholders have not had fair and equitable treatment, but that such changed conditions inure to the benefit of the stockholders of which the Missouri Pacific Trustee is one.

SUMMARY OF THE ARGUMENT.

I.

The Plan of Reorganization of the Debtor does not provide for fair and equitable treatment for the claims and interests of the Debtor's General Mortgage Bondholders.

II.

The Senior Bondholders, having been paid in full, are not entitled to receive additionally the value of the Rio Grande Junction Railway Bonds purchased pursuant to an Order of the District Court.

III.

The Senior Bondholders are not entitled to receive, in addition to what they receive under the Plan, the value of the equity in the stock of Utah Fuel Company.

IV.

The Senior Bondholders, having been paid in full, are not entitled to receive current assets in excess of necessary working capital.

V.

The Plan of Reorganization does not reflect the changed economic conditions surrounding the operation of the Debtor.

VI.

The properties of the Debtor cannot be successfully operated independently under any plan of reorganization.

ARGUMENT.

I.

The Plan of Reorganization for the Debtor Does Not Provide for Fair and Equitable Treatment for the Claims and Interests of the Debtor's General Mortgage Bondholders.

On November 1, 1935, the Debtor's total debts senior to the claim of the General Bondholders was slightly over $101,000,000. The General Bondholders' claims at that time were approximately $30,000,000, making the total of the two claims approximately $131,000,000. Any one of the ten plans of reorganization prior to the final one fixed the value of the property at more than enough to satisfy the claims of all bondholders in full, as of the date this proceeding was instituted. During the ten years following November 1, 1935, the claim of the Senior Bondholders became more than $139,000,000, and the claim of the General Bondholders amounted to more than $43,500,000, making a total of more than $182,000,000 for these two classes of claims (R. 248, 249).

The income of the Debtor during this period was approximately $50,000,000. This income was not used in the payment of interest on the senior claims, but in making permanent and lasting improvements to the facilities of the Debtor. For this purpose, more than $43,000,000 were capital expenditures. As a result, the position of the General Bondholders has dropped from a 100 per cent participation of their claims to a mere 10 per cent.

The Senior Bondholders, by reason of the foregoing, received practically the exclusive benefit of capital expenditures in the sum of $43,000,000, and in addition the claim of such Senior Bondholders, by reason of accumulated interest, increased from $101,000,000 to $139,000,000. To all

intents and purposes, if the Plan of Reorganization is to stand, in a large measure eliminating the General Bondholders from participation in the reorganization of the properties of the Debtor, then such Plan of Reorganization that brings about the foregoing result must conform in every respect to the law of the land, and we shall hereinafter show that such Plan of Reorganization denied to the General Mortgage Bondholders that fair and equitable treatment that the statute requires.

II.

The Senior Bondholders, Having Been Paid in Full, Are Not Entitled to Receive Additionally the Value of the Rio Grande Junction Railway Bonds Purchased Pursuant to an Order of the District Court.

The United States Circuit Court of Appeals correctly held (R. 247) that:

> "The Senior Bondholders were paid in full. They received all the new securities and most of the common stock. Ninety per cent of the General Bondholders' claims were wiped out. They received only a small amount of common stock, ten per cent of their total claim."

Since by the allotment of new securities the Senior Bondholders were paid in full, it seems clear that they should not receive under any Plan of Reorganization, assets of the Debtor in addition to payment in full of their claims.

By Order No. 484, filed September 16, 1943 (R. 264), the District Court permitted the Trustees of the Debtor, out of funds in their hands as Trustees, to purchase for the benefit of the trust estate the First Mortgage 5% Bonds

due December 1, 1939, of The Rio Grande Junction Railway Company. The Rio Grande Junction Railway Company (R. 250) is a wholly owned subsidiary of the Debtor. It had bonds outstanding in the hands of the public for the payment of which the Debtor was liable, totaling $2,758,333. This claim was senior to that of the General Bondholders. The Circuit Court of Appeals, in dealing with this Order of the District Court to purchase the Junction Bonds for the benefit of the trust estate, said, (R. 250):

> "The plan set aside securities for the payment of this claim. In an order dated September 13, 1943, the District Court directed the trustee to pay this claim with some of the surplus cash on hand, and retained the securities which were to be used in the payment thereof in the treasury of the company. The court treated the transaction as a purchase of securities rather than a payment of a debt. This is a play upon words, and, in any event, is immaterial to the issue. The fact remains that the new capitalization provided securities for the payment of these bonds. The value behind these securities in no wise belonged to the Senior Bondholders, because they had been paid in full. When surplus cash was used to pay this claim, the value behind the securities set aside for that purpose remained undistributed. Since the Senior Bondholders had been satisfied in full, this undistributed value in all equity and fairness belonged to the General Bondholders. Any plan which does not give it to them does not comply with the requirements of Section 77 (e) of the Act."

The Senior Bondholders having been paid in full, if the Plan of Reorganization is made effective, will undoubtedly receive, in addition to being paid in full, as part of the securities of the new company, the value of these Junction Bonds purchased pursuant to an Order of the District Court.

III.

The Senior Bondholders Are Not Entitled to Receive, in Addition to What They Receive Under the Plan, the Value of the Equity in the Stock of Utah Fuel Company.

The stock of the Utah Fuel Company is pledged under Rio Grande Western consolidated mortgage, subject to the right of redemption (R. 123).

The Commission, in its original report (R. 52), found that the balance sheet of the Utah Fuel Company as of December 31, 1936, showed assets of $15,171,943, par value of stock outstanding $10,000,000, and corporate surplus of $2,652,839.

The Commission also refers to an appraisal of the property made by the Trustee of the Rio Grande Western consolidated mortgage which indicates a going concern value of $4,653,720.

In its second supplemental report (R. 123) the Commission, in dealing with this Utah Fuel Company's stock, stated:

> "The company's earnings are not of record since 1936, in which year, and in 1935, small amounts of net income were reported. The debtor, in its original earnings formula, credited the Rio Grande Western consolidated mortgage district with an income of $83,333 a year from the fuel company."

The Circuit Court of Appeals calls attention to the fact (R. 252) that:

> "The Commission's amended order disposes of this collateral in the following manner: * * * the trustee under the mortgage securing the R. G. Western Consolidateds (shall) be permitted to obtain the release of the equities * * * in the stock of the Utah Fuel Company, and distribute the stock among the holders.

of bonds in any manner acceptable to them, or to enforce its rights as pledgee of the stock, * * * (of the Utah Fuel Company) the proceeds recovered to be distributed to the holders of the bonds.' ".

Then the Court finds (R. 252) as follows:

"There can be no question as to the duty resting upon these claimants to credit the value of this collateral upon their claim before sharing in the securities of the reorganized company. They were entitled only to full payment. If the new securities which were assigned to them satisfied their (fol. 260) claim in full, then the plan which permitted them to retain in addition this collateral would be inequitable and unfair to junior creditors.".

Since the Senior Bondholders make no point, or do not contend, that they have illegally been dealt with, it must be assumed that the claim of such Senior Bondholders has been paid in full and that in addition to such payment in full they are clearly not entitled to the value of this collateral in question.

IV.

The Senior Bondholders, Having Been Paid in Full, Are Not Entitled to Receive Current Assets in Excess of Necessary Working Capital.

As appears from the opinion of the Circuit Court (R. 247), as of December 31, 1944, the working capital of the Debtor had increased from a deficit of $9,727,230 as of December 31, 1935, to a surplus of $12,125,863.50.

The Circuit Court further found that any plan which fails to take this situation into account and which gives the Senior Bondholders their claims in full by substantially delivering the road to them and also gives them the surplus cash actually on hand, and further enables

them to receive in addition the excess war profits which are reasonably sure to come, is inherently inequitable and unfair so long as there are claims of creditors whose claims are not fully satisfied.

The Circuit Court further found (R. 248): "The conclusion is inescapable that on either June 14, 1943, or December 31, 1943, there were on hand surpluses greatly in excess of what was necessary for the proper operation of the railroad."

Attention is also called by the Circuit Court to the fact (R. 251) that debts due Senior Bondholders include equipment obligations of $5,758,000. That under the Plan, these claims are to be paid with new securities and are thus satisfied before the General Bondholders receive anything. As of December 31, 1944, the equipment obligations had been reduced to $4,540,000, which resulted in a decrease in these obligations of $1,218,000. The new securities set apart for the payment of this sum will not be needed.

Petitioners in their brief, at pages 31 to 55, take issue with the finding of the Circuit Court that they have been paid in full.

At page 34 of their brief, petitioners contend that it is not enough that the Senior Creditors retain some seniority of position, as the Circuit Court apparently thought, but they are entitled to receive realizable value in the full amount of their claims before the General Mortgage Bonds are entitled to receive anything, citing: **Case v. Los Angeles Lumber Products Co., Ltd.**, 308 U. S. 106, and **Consolidated Rock Products Co. v. DuBois**, 312 U. S. 510.

Then petitioners say: "If full compensation is to be attained in fact, such value must reflect what people will probably pay, either now or within some assured future."

This is a unique and startling doctrine. Certainly the Commission, in allocating securities to the payment of the claims of the Senior Bondholders, is not required to

find the market value of such securities as of the date allocated or predict their value at some future date.

At page 40 of their brief, petitioners assert that where a Junior Creditor complains, it would frustrate the Congressional scheme to hold that, while the rights of a creditor who receives nothing are determined as of the time of the Commission's finding, the rights of the creditor who receives 10 per cent of his claim are determined as of some other date, and that the Congressional purpose requires that the same test be applied in each case.

A sufficient answer to this contention is that the Senior Bondholders elected to be bound by the "time of the finding" by the Commission, while the General Mortgage Bondholders did not.

Petitioners admit, at page 40 of their brief, that the District Court, in approving the plan, is entitled to consider any changes of condition to that time. If, as stated by petitioners at page 41 of their brief, the validity of the Commission's action is to be judged as of the date of the Commission's action, but that evidence may be considered of latter changes to the time of approval, or, where a class dissents, to the time of confirmation, then the point made by petitioners that the "time of the finding" is decisive in these appeals is erroneous.

It is obvious that at the time a plan of reorganization comes before a court for approval or confirmation, accumulated cash on hand may have reached such volume as to preclude the delivery of this cash to bondholders whose claims have been satisfied, and whether such accumulation has reached such a point is for the court to determine. Conceivably, such excess of cash may accrue between the date the Commission formulates a plan and such plan comes before the court for confirmation. If such were the case, certainly the court would not be outside of its jurisdiction to pass upon this feature. It may be, as stated in the case of **In re New York, New Haven & Hartford R.,**

147 F. 2d 40, that: "It is for the informed judgment of the Commission rather than for the courts to determine the sufficiency of any cash reserve to meet the uncertainties ahead." It certainly is a proper function of the court to see that the action of the Commission is not arbitrary and has not been rendered obsolete by evidence following the formulation of the plan by the Commission.

It is conceded by petitioners, at page 45 of their brief, that on December 31, 1944, cash, plus the excess of Government obligations over accrued tax liabilities, equaled $12,000,000, and that net current assets (including the cash and Governments) were $16,000,000. Certainly this situation called for a judgment by the court.

At page 51 of their brief, petitioners take exception to the finding of the Circuit Court that the new securities allocated to the Senior Bondholders would satisfy their claims; or, as stated by petitioners, "would have a value equal to their face amount," and asserts that such finding was made without reference to any price at which new common stock might be sold, either now or at any foreseeable time. Stated another way, the position of petitioners seems to be that when securities are allocated to the Senior Bondholders in settlement of their claims, unless the Commission find that such securities have a market value equal to the face value of their claims at the time it formulates the plan of reorganization or fixes a future date at which time such securities would equal the face value of their claims, the court is without jurisdiction to find that such Senior Bondholders have been paid in full. By this contention they ask that the Commission be required, in formulating a plan of reorganization of a railroad, to enter the domain of speculation and allocate to the payment of the claims of Senior Bondholders securities having regard to what the Commission thinks is their market value rather than their face value. Our attention

has been called to no such action in formulating any plan of reorganization for any debtor.

If the Senior Bondholders have not been paid in full, then what was done by the Commission violates the rule laid down in the case of **Northern Pacific R. v. Boyd**, 228 U. S. 482, and petitioners make no such contention. They have accepted the Plan of Reorganization, seek to make it effective, and cannot now be heard to say, in this court, that their claims have not been satisfied.

V.

The Plan of Reorganization Does Not Reflect the Changed Economic Conditions Surrounding the Operation of the Debtor.

During the five years, 1927-1931, since the Debtor controls the Denver & Salt Lake, the average system income available for interest was $8,103,881. During the four years, 1932-1935, the average system income available for interest was $3,606,921. During the three years, 1936-1938, the average system income available for interest was $1,128,869 (R. 84).

In its Third Supplemental Report, dated June 14, 1943, on the claims outstanding; the Commission fixed the capitalization of the new consolidated company at $155,173,127 (R. 156).

Under such capitalization, total fixed interest charges would approximate $1,694,941, prior contingent-interest charges $498,318, and contingent-interest charges $1,364,133; and, including the payments to sinking funds and the capital fund, the total charges before dividends on the preferred stock would be $4,584,689.

In its original report (R. 84) the Commission, after setting forth the earnings of the Debtor, stated:

"There is no evidence in the record indicating any

probability that the carriers can bring their earnings up to the 1930 level or to that of the 1927-31 average; and in our opinion such former earnings should not be relied upon as the measure of an earning power justifying a finding that the equity in the debtor's stock has a value."

Having regard to the capitalization of the new consolidated company heretofore referred to, it is obvious that the Commission was influenced primarily, not by the earnings of the Debtor prior to the depression years and not by the earnings of the Debtor following the end of such depression, but by the earnings during the depression.

Sub-section (e) of Section 77 of the Bankruptcy Act, as amended, provides in part that: "The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present and prospective, and all other relevant facts." It is the opinion of this respondent that the Commission failed to give effect to the requirements of the statute just above set out. It obviously relied on earnings during the depression period and fixed the value of the properties of the Debtor accordingly. For the year ending December 31, 1942, there was available for interest $17,044,420.39, and a net income of $11,306,965.60 (page 4, Annual Report for the year ended December 31, 1942, transcript of record, financial statements).

For the year ending December 31, 1943 (page 11, Annual Report, transcript of record, financial statements), the earnings available for interest were $11,873,667.94, with net income of $5,907,759.81. And for the year ending December 31, 1944, earnings available for interest amounted to $8,490,992.45, with net income of $2,505,572.25 (page 1, Annual Report, transcript of record, financial statements).

It will be observed, of course, that the net income shown

in the annual reports heretofore referred to are based upon the capitalization of the old company and not on the capitalization proposed by the Commission in its Plan of Reorganization.

To justify its failure to give effect to the increased earnings of the Debtor following the end of the depression, the Commission stated in its Third Supplemental Report (R. 159):

> "The debtor's earnings in 1942 are recognized, but the uncertainties surrounding the economic situation negative any assurance of a long continuation of such earning power. Under the present program, the expenditures necessary to handle the abnormally heavy traffic incident to the war effort will be paid for out of the income produced by that traffic. It is not probable, in our opinion, that the debtor will have any large amount of excess revenue from this special traffic after these and other necessary charges are made."

From the foregoing, it appears that the Commission assumed that the earnings of the Debtor for the years 1943, 1944 and thereafter, would be dissipated by certain expenditures necessary to handle the traffic in question.

The operating results for the years 1943 and 1944 indicate just how wrong the Commission was when it acted upon such an assumption.

Just how the Commission arrived at the conclusion as stated in its final report, that expenditures necessary to handle the heavy traffic incident to the war would dissipate the income produced by that traffic is not understood in view of what the Commission said in its second supplemental report (R. 118), as follows:

> "The evidence adduced at the further hearing shows that the improvement program has been substantially

completed. From the appointment of the Debtor's trustees on November 1, 1935, to March 31, 1941, a total of $22,916,051 was expended on the Debtor's property, of which $17,504,246 was chargeable to capital account. The ratios of maintenance to total revenue had been 35.12 in 1935, 41.09 in 1936, 46.83 in 1937, and 39.09 in 1938. The Debtor believes that the improvements already made, together with the acquisition of new Diesel switch engines and road engines costing $4,000,000 will produce a large and permanent reduction in operating costs."

In view of the foregoing, the conclusion of the Commission as found in its final report, that expenditures necessary to handle heavy traffic would absorb substantially the income derived therefrom is clearly without foundation.

Also, the improvements to the property of the Debtor were before the Court when it confirmed the Plan, together with facts indicating conclusively the ability of the Debtor to handle expeditiously and economically traffic that might be expected to move over its lines.

This is shown by the following excerpt from the opinion of the Court approving the Plan (R. 195) when reference is made to the action taken by the Trustees when they were placed in charge of the property:

"The Trustees promptly drew up an improvement program and prosecuted it at a cost through and including the first half of 1943 of roughly $40,000,000. This includes $1,065,000 for the installation of centralized traffic control on 115 miles of the main line—mostly west of Dotsero. The net result of this alone was to enable the road to give an operation efficiency on a single track equal to about 90% of what could have been accomplished on a double track operation. $104,000 was spent on automatic block signals on the Salt Lake Western between Bond and Dotsero, and new slag ballast installed on 413 miles of roadbed,

and 436 miles of new rail was laid at a cost of $6,968,500. Main terminals and freight yards were enlarged and improved at a cost of over $1,700,000. In addition many line and grade changes were made, passing tracks installed at various points, and a considerable amount of roadway and work equipment acquired."

In the **Milwaukee** case, supra, this Court held that the question of improved economic conditions was one for the Court as well as for the Commission. In the **Milwaukee** case, the Court said:

"As we have indicated in the Western P. R. Corp. Case the power of the District Court to receive additional evidence may aid it in determining whether changed circumstances require that the plan be referred back to the Commission for reconsideration."

The Commission, in its final report, had before it operating results for only the first part of the year 1943, while the District Court when confirming the Plan had before it such results not only for the year 1943, but for substantially all of the year 1944, and such figures indicated that the increased earnings of the Debtor are not ephemeral, but rest upon rather a substantial basis and may not lawfully be entirely disregarded.

The question of the effect of changed economic conditions and circumstances upon proceedings before the Commission was before the Supreme Court in the case of **Atchison, T. & S. F. R. Co. v. U. S.**, 284 U. S. 248. In that case the Court said:

"It is plain that a record which was closed in September, 1928—relating to rates on a major description of the traffic of the carriers in a vast territory—cannot be regarded as representative of the conditions existing in 1931. That record pertains to a different

economic era and furnishes no adequate criterion of present requirements. While the effects of the widespread economic disturbance have had a progressive manifestation, they had been sufficiently revealed in February, 1931, when the second petition for rehearing was made, to compel the conclusion that the record of 1928 afforded no sufficient basis for the order of the Commission."

It is clear that economic forces in effect for three years and in effect when the Court confirmed the Plan have made the record before the Commission **irresponsive to changed economic conditions.** All of the facts connected with this proceeding indicate that if changed economic conditions are given their proper effect in connection with a Plan of Reorganization of the properties of the Debtor, the finding of the Commission as to the value of such properties cannot stand. The conclusion is inescapable that the Commission formulated a Plan of Reorganization of the Debtor and the District Court confirmed it upon the erroneous assumption that the value of the combined properties of the Debtor could be established by giving effect only to earnings of the Debtor, not throughout all of the past years previous to and during the bankruptcy, but only through those years in which there existed an economic depression the equal of which this country had never before experienced.

It is clear that both the Commission and the District Court were of the opinion that while industry as a whole might continue on a stable basis with earnings comparable to those before 1930, the earnings of railroads after the war would revert to those of the depression years. It is the contention of this respondent that the Commission and the Court erred in so holding and that because of this fact, the Plan of Reorganization should not be permitted to become effective.

In the **Milwaukee** case, supra, the Supreme Court said:

> "The basic question in the valuation for reorganization purposes is how much the enterprise in all probability can earn."

The Commission has in a somewhat arbitrary manner assumed that the properties of the Debtor when reorganized will have lower earnings than the facts in this proceeding justify and such findings operate to the detriment of the General Creditors and stockholders of the Debtor.

We have heretofore referred to the fact that as of November 1, 1935, the total debts of the Debtor senior to the claims of the General Bondholders approximated $101,000,000 and that the claims of the General Bondholders at that time were approximately $30,000,000, making the total of the two claims approximately $131,000,000.

As of December 31, 1936, the Commission found (R. 36) that on the basis of the original cost of the system properties, the value would be $178,024,641, and in this connection, we refer to the investment in road and equipment of the several corporations as shown on the consolidated balance sheet of December 31, 1936, in the grand total of $238,750,511 (R. 35).

Beginning in 1925 (R. 738), the Debtor inaugurated its own five-year improvement plan and during the period from January, 1925, to the beginning of the trusteeship, $40,000,000 were spent in rehabilitating the property of the Debtor. $30,000,000 of the total amount expended were capital expenditures and something over $9,000,000 were charged to operating expenses.

We have heretofore referred to the fact that the Trustees, following bankruptcy, also rehabilitated the properties of the Debtor (R. 195) by spending approximately $40,000,000 capital expenditures.

The Commission in its findings of value obviously ignored the foregoing figures.

As of November 1, 1935, since the combined debts of the Debtor approximated $131,000,000, based on the findings of the Commission (R. 69) that of December 31, 1936, the cost of reproduction of the system properties, less depreciation, was $147,717,268, the value of the equity of the stockholders approximated $16,000,000.

VI.

The Properties of the Debtor Cannot Be Successfully Operated Independently Under Any Plan of Reorganization.

The Commission has long recognized that it is in the public interest for the Missouri Pacific to occupy the status of one-half owner of the Debtor. **Denver & Rio Grande Reorganization**, 82 I. C. C. 745; **Acquisition by Missouri Pacific of D. & R. G. W. Common Stock**, 90 I. C. C. 161. In the case last cited, the Commission said:

> "The record supports the contention of the applicant that its proposed acquisition and the use of the proceeds in connection with the termination of the receivership of the Denver Lines in the manner required by the agreement and plan of reorganization will be mutually beneficial to the applicant and the new Denver company and consequently bring about the furnishing of more efficient and better service to the people of the communities served by the lines of the two companies."

All concerned in the reorganization of the properties of the Debtor recognize that if such properties are to be successfully operated, reliance must be had on bridge traffic. The District Court, in approving the Plan of Reorganization (R. 203), said:

> "True there has been a tremendous increase in bridge traffic of the Rio Grande over a period of years. In 1920 the percentage of bridge traffic to total

tonnage was 6.95%. This has steadily increased year by year until 1942, when the percentage of bridge traffic to total traffic amounted to 35.93%, out of a total tonnage of 5,496,833 tons, and for 1943 is estimated at 40% of 7,000,000 tons. Without this business this railroad could not begin to support a capital structure of any size."

The District Court erred, however, in the following statement contained in its opinion approving the Plan of Reorganization (R. 205):

> "The court is convinced from its experience with this property through two receiverships that it is for the best interests of this railroad and its security holders that it be maintained as an independent property free of control by any one road or financial group and free to make such deals with its connections as it deems fit."

In the foregoing statement the Court overlooked a well-known fact in the operation of a railroad, that a company depending on bridge traffic cannot deal as it sees fit with its connections. And this is especially true of the properties of the Debtor. The petitioners, in their brief at page 4, call attention to through transcontinental routes competitive with any route of which the Debtor might form a part, such as, the Great Northern, Northern Pacific, Milwaukee, Union Pacific, Southern Pacific, Rock Island and Santa Fe. All of these lines can ignore the operation of the properties of the Debtor. It follows, therefore, that the Debtor must have a favorable connection east and west, such as, the Western Pacific and the Missouri Pacific, if it is to maintain its status as a participant in bridge traffic moving over transcontinental routes. These connections are an asset of the Debtor which the Plan of Reorganization ignores.

In the **Western Pacific case**, supra, this Court referred to the recommendation of the President in his message of

June 7, 1935, to Congress, recommending amendments to Section 77 of the Bankruptcy Statute, and referred with approval to Senate Report 1336, 74th Congressional Session, in connection with such amendment, as follows:

> "The amendments to Section 77 leave unimpaired the power and the duty of the Commission and the Courts to deal with the most important feature of all reorganization plans, that of control of the reorganized company, and similarly the Commission and the Courts will continue to have the power and the authority of making that thorough investigation which is necessary to assure sound and reliable control for bankrupt companies when they emerge from the Courts, in the place of the type of control under which some railroads have been wrecked."

The foregoing indicates that it is the function of both the Commission and the Courts to examine into this matter of control of reorganized companies and certainly these proceedings are such as to require consideration of that character.

The Commission was without a legal basis to formulate an opinion as to the probable future earnings of the Debtor when by the Plan of Reorganization it practically wiped out the lines of the Missouri Pacific, the Denver and the Western Pacific as a transcontinental route made up of affiliated companies.

The value of the Debtor's property and the interests of the Missouri Pacific Trustee as a stockholder cannot properly be expropriated on the basis of an economic judgment as to value which has now in the light of known events become wholly obsolete.

CONCLUSION.

The period of the Court's administration has been lengthened by controversies between creditors and the Plan proposes that the creditors' claims shall be increased by

accumulating interest during the period of delay occasioned by their controversies and that the equity of junior interests and stockholders should be absorbed to compensate them for such delay. Such seems plainly an unfair and inequitable result. Petitioners, at pages 109, 110, of their brief, refer to the fact that this reorganization has already been long considered by the Commission and the courts, and pray that it may move forward to its completion in accordance with the congressional policy of prompt action in these matters colored by the public interest.

The only congressional policy of which we are aware is the policy stated in the statute and certainly this proceeding is not colored by public interest that prevents fair and equitable treatment.

It is the position of the Missouri Pacific Trustee that, although the Circuit Court erred when it held that the equities of the stockholders of the Debtor were without value, this proceeding should be referred back to the Interstate Commerce Commission in accordance with the direction of said Circuit Court to the end that such Commission, with the aid of all interested parties, may formulate a new plan that will not only provide for fair and equitable treatment of the claims of the junior bondholders, but also recognize that the equities of the stockholders in view of all the facts surrounding this proceeding have a substantial value.

Respectfully submitted,

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SUPREME COURT OF THE UNITED STATES.

Nos. 278, 279, 280, 281 and 282.—October Term, 1945.

Reconstruction Finance Corporation; Insurance Group Committee; Guaranty Trust Company of New York, Trustee, Rio Grande Western Railroad Company Consolidated Mortgage; Central Hanover Bank and Trust Company, Trustee, Rio Grande Western Railroad Company First Trust Mortgage; United States Trust Company of New York, Trustee, Denver and Rio Grande Railroad Company Consolidated Mortgage; and The Chase National Bank of the City of New York, Trustee, Denver and Rio Grande Western Railroad Company Refunding and Improvement Mortgage, Petitioners,

278 *vs.*

The Denver and Rio Grande Western Railroad Company, et al.

Same,

279 *vs.*

The Denver and Salt Lake Western Railroad Company, et al.

Same,

280 *vs.*

City Bank Farmers Trust Company, Trustee Under the Debtor's General Mortgage.

Same,

281 *vs.*

The Denver and Rio Grande Western Railroad Company, et al.

Same,

282 *vs.*

Guy A. Thompson, Trustee, Missouri Pacific Railroad Company, Debtor.

On Writs of Certiorari to the United States Circuit Court of Appeals for the Tenth Circuit.

[June 10, 1946.]

Mr. Justice Reed delivered the opinion of the Court.

The petitioners in these five cases are the owners of claims against the debtor, Denver & Rio Grande Western Railroad Company, or against a secondary debtor, the Denver & Salt Lake

Western Railroad Company. The respondents are the two debtors just named; City Bank Farmers Trust Company, Trustee under the General Mortgage of the principal debtor; and the Trustee of the Missouri Pacific Railroad Company, a large owner of common stock of the principal debtor.

The debtors sought reorganization in the District Court of the United States for the District of Colorado under Section 77 of the Bankruptcy Act,[1] on November 1, 1935. The Interstate Commerce Commission approved the plan of reorganization under consideration in this review on June 14, 1943.[2] The District Court approved the plan October 25, 1943.[3] It was then submitted by the Commission to the creditors of the classes deemed entitled to vote for acceptance or rejection of the plan and a certificate of the result filed in the District Court on July 15, 1944. All classes of voting creditors approved the plan as required by Section 77 except the holders of the Denver's General Mortgage bonds.[4] On November 1, the District Court held the rejection of the plan by the holders of the General Mortgage was not reasonably justified[5] and thereafter confirmed the plan on November 29, 1944. Section 77(e).

The plan provides for reorganization as of January 1, 1943, by the Denver by adjustment of its assets to its liabilities with or without a consolidation with the Salt Lake and the Salt Lake Western to form a system. The stock of the latter road is held by the Denver. There are no bonds. As no ruling that we are asked or required to make turns upon whether the reorganization is with or without the suggested consolidation, we need not give further consideration to possible differences. In either case, creditors with secured claims against the reorganized roads or against their property were left undisturbed or allocated new securities of the new company, consisting of first mortgage and income bonds, preferred and common stock, in lots, in face amount of the secured claims except for the General Mortgage issue, that the

[1] 11 U. S. C. § 205.

[2] The plan is printed in Denver & R. G. W. R. Co. Reorganization, 254 I. C. C. 349, 385. See for former decisions of the Commission in this reorganization, 235 I. C. C. 515; 239 I. C. C. 583; 254 I. C. C. 5.

[3] C. C. H. Bankruptcy Law Service ¶ 54,562.

[4] The Denver & Rio Grande Western Railroad Company is referred to herein as the debtor or the Denver; The Denver & Salt Lake Western Railroad Company as Salt Lake Western; The Denver & Salt Lake Railway Company as the Salt Lake; The Rio Grande Junction Railway Company as the Junction.

[5] In Re Denver & R. G. W. R. Co., 62 F. Supp. 384.

Commission and District Court determined, through adoption of the plan, were fair and equitable in the light of the respective priorities, liens and collateral of the various secured claims. All of the securities were given a par value. Interest partly fixed and interest partly contingent on earnings was used to gain play in annual charges. The plan eliminated unsecured claims and allocated common stock in face amount of ten per cent of their claim to General Mortgage bonds of the debtor. Its stockholders received nothing. It was determined that the aggregate of the securities in the plan represented the value of the properties for reorganization purposes and that through prospective earnings there was adequate coverage for the charges.[6]

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[6] 254 I. C. C. at 338 to 357.

Full details appear in the plan, note 2, *supra*, as well as explanation of certain items in the following tables. The tables are printed to give the reader a convenient summary of the plan. 254 I. C. C. 382-83.

CAPITALIZATION AND ANNUAL CHARGES.

	On basis of consolidation with Denver & Salt Lake		*Denver & Rio Grande Western without Denver & Salt Lake*	
	Principal	*Annual Charges*	*Principal*	*Annual Charges*
Equipment-trust obligations	$5,758,000	$139,989	$5,758,000	$139,989
Chase National Bank note	2,158,458	45,722	2,158,458	45,722
R. F. C. claim	.....	.....	13,900,605	556,024
Denver & Salt Lake first-mortgage bonds, 4 percent interest	1,500,000	60,000	.....	.....
Denver & Salt Lake income bonds, 3-1 percent interest	9,734,000	292,020	.....	.....
	19,150,458	537,731	21,817,063	741,735
New first-mortgage bonds, 3-1 percent interest	38,573,680	1,157,210	33,373,680	1,001,210
Total fixed interest	57,724,138	1,694,941	55,190,743	1,742,945
Capital fund, maximum payment	.....	750,000	.....	750,000
Prior contingent interest, 4 percent	.....	498,318	.....	348,978
Sinking fund for first-mortgage bonds, one-half of 1 percent	.....	200,489	.....	182,323
		3,143,748		3,024,246
New income bonds, 4½ percent	29,750,184	1,364,133	21,049,579	972,606
Sinking fund for income bonds, one-fourth of 1 percent	.....	76,808	.....	58,527
Total debt, interest, payments to funds	87,474,322	4,584,689	76,240,322	4,055,379
New 5-percent preferred stock, par value $100	32,531,220	1,626,561	32,126,120	1,606,006
New common stock, par value $100	35,167,585	.....	35,167,585	.....
Total capitalization	155,173,127	.....	143,528,027	.....

Respondents sought review in separate appeals from the order of approval or the order of confirmation or both to the Circuit Court of Appeals for the Tenth Circuit. That court reversed the District Court on all appeals and remanded the reorganization proceedings to the Interstate Commerce Commission for further consideration with the statement, 150 F. 2d 28, 40,

> "Nothing in the opinion shall prejudice or foreclose the rights of the parties to propose a new plan of reorganization or the power of the Commission to formulate, approve, and certify a new plan of reorganization in the light of any relevant facts presented to the Commission in any proceeding under 11 U. S. C. Sec. 205(d)."

DISTRIBUTION OF NEW SECURITIES PER $1,000 OF PRESENT BONDS WITH ACCRUED INTEREST.

	First mortgage bonds	*Income bonds*	*Preferred stock*	*Common stock*
Rio Grande Western first trusts ($15,190,000)	$970.20	$349.80	.....	.....
Rio Grande Western consolidated's ($15,080,000)	.....	266.00	$970.90	$93.10
Junction firsts ($2,000,000)	1,061.96	317.21	.....	.....
Denver & Rio Grande consolidated 4's ($34,125,000)	318.92	217.08	321.60	482.40
Denver & Rio Grande consolidated 4½'s ($6,382,000)	329.03	223.97	331.80	497.70
Refunding and improvement 5's ($12,000,000)	250.01	159.61	310.75	692.13
Refunding and improvement 6's ($2,000,000)	264.61	168.94	328.90	732.55
General 5's ($29,808,000)	.....	.....	.....	146.10

CLAIMS.

	Claims as of Jan. 1, 1943	*Undisturbed or extended*
Equipment obligations	$5,758,000	$5,758,000
Rio Grande Western first trust 4's	20,050,800	.....
Rio Grande Western consolidated 4's	20,056,400	.....
Rio Grande Junction first 5's	2,750,333	.....
Denver & Rio Grande consolidated 4's	45,727,500	.....
Denver & Rio Grande consolidated 4½'s	8,823,115	.....
Refunding and improvement 5's	16,950,000	.....
Refunding and improvement 6's	2,990,000	.....
General-mortgage 5's	43,548,155	.....
Chase National Bank note	2,158,458	2,158,458
R. R. Credit Corporation note; paid May 17, 1943	.....	.....
R. F. C. notes	13,900,605	.....
Unsecured claims, approximate	440,000	no equity
Total, Denver & Rio Grande Western	183,161,366	7,916,458

By this remand, the Commission was empowered to proceed anew to consideration of the reorganization in all its phases, § 77(e), including those steps previously taken and approved by the opinion of the Circuit Court of Appeals.

That court approved the valuation of the debtor reached mainly by the use of present and prospective earnings. It held that the valuation adopted need not reflect necessarily the money spent for improvements during the trusteeship for reorganization. 150 F. 2d 35. The soundness of these conclusions is fully supported by the *Western Pacific* and *Milwaukee* cases.[7] The Circuit Court further held that the Commission was justified in refusing to reopen the hearings just before the entry of its order of June 14, 1943, approving the plan, to hear evidence of the then existing economic conditions and the 1943 earnings of the debtor.[8]

The reversal came from the Circuit Court's holding, contrary to the Commission and the District Court, that free cash in excess of operating capital needs and large earnings from war business after the date of the plan should be for the benefit of the General bondholders. 150 F. 2d 35-38. That court further held that decreases in debt by cash payments, with the consequent reduction of securities that were required to be issued under the plan to cover such debt claims, should inure to the benefit of the same General bondholders. 150 F. 2d 38-39. The Circuit Court disagreed also with the treatment of certain collateral deposited behind the First Consolidated Mortgage of the Rio Grande Western Railway Company and secondarily behind other issues of the debtor. This is the Utah Fuel stock issue hereinafter discussed. These differences from the conclusions of the District Court led the Circuit Court to hold that the General bondholders were "reasonably justified" in rejecting the plan and that the District Court was without authority to confirm the plan over their veto. § 77(e).

Petitioners on July 30, 1945, sought a writ of certiorari to review these rulings of the Circuit Court and, on account of the importance of the issues in the administration of railroad reorganization under Section 77, we granted their petition on October 8, 1945. — U. S. —.

[7] Ecker v. Western Pacific R. Corp., 318 U. S. 448, 477-83; Group of Investors v. Milwaukee R. Co., 318 U. S. 523, 539-41.

[8] Cf. 318 U. S. at 543.

The briefs of all the parties here restate the questions presented in the petition for certiorari according to the emphasis the particular party places upon points of controversy. After a general consideration of the background of the plan and respondents' contentions to support the judgment besides the defenses applicable to petitioners' certiorari, we shall give attention to each of the just stated disagreements between the district and appellate court. This will cover the points under review.

The basic problems of railroad reorganization under Section 77 of the Bankruptcy Act have been so recently considered by this Court in the *Western Pacific* and *Milwaukee* cases that only a summary reference to their conclusions attacked by respondents need be made now. No new enactments have changed the law since those decisions on March 15, 1943. The complexities of the reorganization of a railroad with responsibility to the public and obligations to its security holders were recognized. The impossibility without destruction of efficiency and values of reversing the process of integration to restore the parts that now make up the whole of a system of their original operational function was understood. The various bond issues with different and often overlapping liens, with competing claims for allocation of earnings pending reorganization, presented hard problems for legislative solution. A fair, administratively practical and lasting method was sought. By provisions for adjustment of creditors' claims, Congress intended to avoid the delays, costs and sacrifices of liquidation.[9] The agencies employed by Congress to accom-

[9] Applicable provisions of § 77, 11 U. S. C. § 205, are as follows:

"(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; . . .

"(d) The debtor, after a petition is filed as provided in subsection (a) of this section, shall file a plan of reorganization within six months of the

plish reorganizations under Section 77 were the Interstate Commerce Commission and the courts. The answer reached by Congress was that the experience and judgment of the Commission must be relied upon for final determinations of value and of matters affecting the public interest, subject to judicial review to assure compliance with Constitutional and statutory requirements. This was the interpretation of all members of this Court from the language of the act and the evidence of Congressional

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. . . After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (c) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report, the Commission shall state fully the reasons for its conclusions.

"(c) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; . . .

" . . . . If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or reports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: *Provided*, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value; or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any. . . . . *Provided further*, That submission to any class of creditors shall not be necessary if the Commission shall have found, and

purpose in the hearings, reports and discussion.[10] To the courts, Congress confided the power to review the plan to determine whether the Commission has followed the statutory mandates of subsection (e), 318 U. S. at 477, and whether the Commission had material evidence to support its conclusions. 318 U. S. at 477; concurring opinion at 512.

At this point, we restate our conclusion reached in the former cases that the Congressional authority to the Commission to eliminate valueless claims from participation in reorganization is a valid exercise of the federal bankruptcy power. Section 77 was directed at the relief of debtor railroads. Sec. 73, 47 Stat. 1467. Liquidation in depression periods meant that large portions of debts, as well as stock interests in the properties, would be irretrievably lost to their holders, while reorganization on a capitalization that estimated what normal income would support meant the salvage of sound values. We see no more constitutional impedi-

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the judge shall have affirmed the finding that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. . . . The Commission shall certify to the judge the results of such submission.

"Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided*, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e); . . .

"If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

10 318 U. S. at 472, 473, 477; concurring opinion at 512; 318 U. S. at 545.

ment to the elimination of claims against railroad debtors by the Interstate Commerce Commission's determination of values with judicial review as to the sufficiency of the evidence and compliance with statutory standards than we do to their elimination by an accepted bid in a depression market.[11] There is no occasion here to reexamine further these recent holdings of this Court in the *Western Pacific* and *Milwaukee* reorganizations.

In examining the contentions of petitioners as to the alleged errors of the Circuit Court of Appeals, we must approach the problems in accordance with our reviewing authority under Section 77. That section embodies the method that Congress selected in 1933[12] and improved in 1935[13] to put the railroad transportation system of the country in order to meet its debts and perform its duties to the public after the hard years of the recent depression. Our constructions of the chief provisions of the section were handed down in March, 1943. Although the results of reorganizations under the section, as thus construed, have been criticized as unfortunate and changes have been suggested, no different legislation has been enacted.[14] Indeed a different method for reorganization, enacted in 1939 and designed to meet the requirements of railroads not in need of financial reorganization

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[11] 318 U. S. at 475-76; 318 U. S. at 536-39.
Compare Wright v. Union Central Ins. Co., 311 U. S. 273, 279; John Hancock Ins. Co. v. Bartels, 308 U. S. 180, 186; Gelfert v. National City Bank, 313 U. S. 221.

[12] 47 Stat. 1474.

[13] 49 Stat. 911. H. Rep. No. 1283, 74th Cong., 1st Sess., p. 1; S. Rep. No. 1336, 74th Cong., 1st Sess., p. 1; Craven & Fuller, Amendments of Railroad Bankruptcy Law, 49 Harv. L. Rev. 1254. See Ecker v. Western Pacific R. Co., 318 U. S. at 470, *et seq.*

[14] H. R. 5924, 79th Cong., 2d Sess.; Hearings on H. R. 4779, 79th Cong., 1st Sess., Serial No. 13; H. Rep. No. 1828, 79th Cong., 2d Sess., p. 3:

"Although all these laws were intended by Congress for the preservation of our railroads and their ownership, the theory has appeared to prevail that the capitalization of companies in section 77 proceedings should in all cases be drastically reduced. That is what has been done consistently and persistently. Under the past administration of section 77, as that statute was interpreted and applied by the Interstate Commerce Commission and affirmed by the Supreme Court, countless thousands of small stockholders already have been wiped out, and their investments, which would now be of great value, were uselessly destroyed. There are many more thousands upon thousands of such stockholders whose investments are imminently threatened with a like fate, unless Congress promptly enacts legislation to prevent such needless loss. And that loss—aggregating over $2,000,000,000—would be suffered largely by a widely scattered class of citizens (many thousands of whom are employees of these very railroads) who invested their legacies or their savings in one of America's greatest private enterprises, for education of their children, the purchase of homes, or security in old age. It literally may be

of the character provided by Section 77 but only of an opportunity for voluntary adjustments with their creditors, terminated on July 31, 1940, and a comparable provision made in 1942 was allowed to lapse on November 1, 1945.[15] This situation leaves clear the duty of the agencies of the Government entrusted with the handling of reorganizations under Section 77, including this Court, to administer its provisions according to their best understanding of the purposes of Congress as expressed in the words of Section 77 read in the light of the contemporaneous discussion in Congress. Changes in economic conditions cannot effect the powers of the reorganization agencies even though such changes may require a reexamination into the present fairness of the former exercise of those powers.

Valuation. The Denver and Rio Grande Western, the principal debtor, is an important link in transcontinental trasportation.[16]

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said that these stocks were the favorite investments of widows and orphans and of trustees."

S. Res. 192, 79th Cong., 1st Sess.; S. Rep. No. 925, 79th Cong., 2d Sess.; S. 1253, 79th Cong., 2d Sess.; Hearings on S. 1253, 79th Cong., 1st Sess., Voluntary Modification of Railroad Financial Structures; Hearings, on S. 1253, 79th Cong., 2d Sess., Modification of Railroad Financial Structures, Part 2; S. Rep. No. 1170, 79th Cong., 2d Sess., pp. 1-2:

"The bill (S. 1253) enables railroad companies to adjust their financial affairs quickly, economically, and on a business basis. The procedure it provides will reduce any disturbance of their affairs to a minimum, and will provide the maximum of protection for both the railroads and their investors.

"The existing law, section 77, was enacted in 1933, without hearings and without consideration of any subcommittee or committee of the Senate. It was enacted in the belief that it would help railroads to correct their financial affairs. It was found to do the opposite. It has placed in the hands of Government officials extraordinary power, which they had not requested, over 25 percent of the country's railroad mileage—a power which they have exercised:

(1) to demolish every part of the financial and corporate structures of those railroads;

(2) to plan in every respect the financial and corporate future of those railroads;

(3) to pick men to control those railroads; and

(4) to decree the forfeiture of $2½ billion of investments.

"The present bill puts an end to every one of those powers and restores the operation of railroads to their managements and the adjustment of their finances to the companies themselves, with the assistance of their securityholders, where necessary."

See A Critical Analysis of Recent Reorganization Decisions of the Supreme Court of the United States, F. C. Nicodemus, Jr., Hearings on H. R. 4779, subsequently H. R. 5924, 79th Cong., 1st Sess., p. 181.

[15] 53 Stat. 1134; 56 Stat. 787. A bill to extend this act to 1959, H. R. 3429, was passed by the House of Representatives on November 1, 1945, 91 Cong. Rec. 10434; H. Rep. No. 1128, 79th Cong., 1st Sess.

[16] Full details of the properties, the elements of rate making value, the corporate history, the capital structure at the beginning of the reorganization

The recent availability to the debtor of the Moffett Tunnel and the Dotsero Cut-off (1934) improve its strategic position in the competition for "overhead" or "bridge traffic," that is, traffic that is consigned from and destined to points beyond its lines. The traffic originating or terminating on its lines is mixed in character and varies with the general prosperity of the region.

The present Denver, the principal debtor, was organized in 1920. It succeeded the Denver & Rio Grande Railroad Company of 1908 which had in its turn acquired the property of the Rio Grande Western Railway Company, owning the western portion of the present debtor's lines, and of the Denver & Rio Grande Railroad Company of 1886, owning the eastern portion of the present debtor's lines. A connection between the two portions, Rio Grande Junction Railway, is under lease to the debtor which, as lessee and a stockholder, guarantees the Junction bonds. Substantially all of the capital stocks of the Salt Lake and Salt Lake

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proceedings, the traffic and earnings appear throughout the various reports of the Commission, particularly the original report in 233 I. C. C. 515. The location and extent of its properties are succinctly described by the Commission at page 518, as follows:

"The Denver's principal eastern termini are Denver and Pueblo, Colo., at each of which points connection is made with the Atchison, Topeka & Santa Fe Railway and the Colorado & Southern Railway. At Denver connection is also made with the Chicago, Burlington & Quincy Railroad, the Chicago, Rock Island & Pacific Railway, and the Union Pacific Railroad; at Pueblo, also with the Missouri Pacific Railroad, which is the Denver's main outlet to the east.

"On the west the main line of the Denver passes through Salt Lake City and terminates at Ogden, Utah. Connection is made with the Union Pacific at each point; at Salt Lake City the Denver also connects with the Western Pacific Railroad and at Ogden with the Southern Pacific. The interchange with the Western Pacific is more important than that with any other western connection.

"The road owned by the Denver consists of 1,256.6 miles of main line and 1,094.9 miles of branch lines. Operated under lease are the Rio Grande Junction Railway . . . extending from Rifle to Grand Junction, Colo., 62.1 miles, the Goshen Valley Railroad, a branch line 8.8 miles in length, and the Salt Lake Western, extending from Dotsero, on the Denver, to Orestod on the Denver & Salt Lake Railway . . . 38.1 miles. Including these leased lines, the Denver operates approximately 1,357 miles of main lines and 1,104 miles of branch lines. Approximately 771 miles of narrow gage lines are included in the operated mileage.

"In addition to the above-mentioned mileages, the Denver operates over the Salt Lake between Denver and Orestod, 128.6 miles. This line, together with the Salt Lake Western, constitutes the Dotsero cut-off route. The Salt Lake's ownership embraces the line extending from Utah Junction, near Denver, to the western terminus at Craig, Colo., 220.2 miles. For its Denver terminal, the Salt Lake uses, under a lease, the facilities of the Northwestern Terminal Railroad Company. The Salt Lake derives no revenues from the through traffic moving over the cut-off, since all such traffic is handled by the Denver."

Western, and various other branch lines are owned by the debtor.[17] These corporate arrangements for the operations of the debtor have resulted in the assumption or creation by the debtor of the claims of the various issues, listed in note 6, *supra*.

Just after these reorganization proceedings began, December 31, 1935, the debtor's report showed that its long-term debt was $120,541,000, and its current liabilities $24,990,901.63. It had current assets, including cash $1,257,948.43, of $5,966,666.93. At the time the plan became effective, December 31, 1942, the report showed long-term debt of $130,264,826.65 and current liabilities of $14,172,575.50, and in addition deferred liabilities, chiefly matured interest in default of $45,582,132.66. There were current assets, including cash $10,850,149.96, of $20,983,652.54. As of December 31, 1944, these items were: Long-term debt $129,358,337.79, current liabilities $20,539,637.83, and deferred liabilities $55,310,151.80. The current assets were $32,665,501.33, including $19,142,626.96 in cash.

During the period examined the income of the system available for interest was found by the Commission at its lowest in 1936-1938. After adjustment this was $2,893,255. 233 I. C. C. at 552. In 1941 there was $5,019,436. 254 I. C. C. at 10. When the present plan was approved by the Commission in June, 1943, the 1942 income available for interest was recognized but the continuance of such earning power was thought to be negatived by any sound forecast.[18] 254 I. C. C. at 356.

Earnings during the trusteeship were used to improve the debtor railroad. When the vote was taken in 1944, the real estate and equipment account showed charges of $43,291,513 during the trusteeship. An estimated ten million of it was between the Commission's approval of the plan, June, 1943, and the Commission's certification, on July 15, 1944, to the court of the vote by claimants. See 254 I. C. C. at 354 and 382 for explanation of new equipment program to meet the war situation. The retirements are said by the respondent trustee to have been about $13,000,000, leaving a net addition to capital account of $30,000,000.

[17] See Denver & Salt Lake Western R. Co. Construction, 154 I. C. C. 51; 175 I. C. C. 535; 233 I. C. C. at 520.

[18] The reports show the income available for interest as follows:

1942	$17,044,420.39
1943	11,573,667.94
1944	8,157,880.25

Respondents urge that since capitalization was not substantially increased by the Commission between 1938, when the first draft of a plan came from the Commission's staff, and 1943, the junior creditors got little or nothing for this investment. The improvements may have been wise or unwise. That question is not before us. Railroads even in reorganizations must make additions to take care of public needs or to lower operating costs. See 62 F. Supp. 389. The senior bond interest continued to accumulate during this period. As the capitalization was not increased pari passu with the purchases, the holders of junior securities received less participation. The Commission did not consider that the earning prospect justified a greater capitalization than the one given and we think its judgment controls the valuation. As was said by the Circuit Court of Appeals in *In re Denver & R. G. W. R. Co.*, 150 F. 2d at 38:

> "Neither was the Commission compelled to, nor would it be justified in adding the amount of these expenditures to the capitalized value if in the exercise of sound discretion it felt that the reasonable prospective earnings of the road, after the improvements did not justify it. However, in the face of all this, after satisfying in full the claims of the senior bondholders, the plan of reorganization should have made sure that all excess current assets, as well as all excess war profits yet to accrue, would go to the General Bondholders."

The last sentence, we think, has the vice of overlooking the reason the Commission gave common stock to the Seniors. See discussion under *Allocation of Securities*.

We note also the contention that the possibility of a national income much higher and interest rates much lower than before World War II should affect valuation based on prospective earnings. Those factors, we think, were before the Commission when it made its earnings estimate.

The Commission reached its determination of a sound capital structure for the combined properties with these figures on earnings and investments before it. In addition, of course, the Commission had complete statistical information to guide it from its Bureau of Valuation and its other sections dealing with traffic, rates, earnings, interest, et cetera. The discussion by the Commission will be found in its printed volumes listed in note 2. Proceeding upon the principle accepted in the *Western Pacific* and

Milwaukee cases,[19] that capitalization based upon earnings is a permissible method of valuation in reorganization, the Commission fixed $155,173,127 as the sound capitalization. This capitalization under the terms of the issues, with provisions for a capital fund and the sinking funds, carries annual charges at rates varying with the security of $6,211,250 before dividends on common. This present annual charge, plus, let us assume, five per cent annually upon the common, $1,758,379, or a total of $7,969,629, is the basic figure to be applied, with adjustments for the variable factors, to earnings, past or prospective, available for interest and dividends as an aid to determine the fairness of the present valuation. See note 6. The decision was unanimous except for one Commissioner who considered the valuation too high by ten per cent. 254 I. C. C. at 379. There can be no doubt that as of June, 1943, there was ample evidence to justify the valuation made by the Commission.

Allocation of Securities. Within the framework of that valuation, the Commission allotted the available securities to the claimants. Securities, including the common stock, were given a face value. The aggregate was too small to allow anything to former stockholders.[20] Thus they were eliminated from the reorganization.[21] For the holders of the General bonds, common stock was available to the amount of ten per cent only of their claim.[22] A glance at the proposed distribution in note 6 will show that the claimants did not receive all the new senior securities in the strict order of their old priorities.

The value of a lien on a part of a railroad when the valuation is made from earnings cannot be fixed solely on a mileage basis. Nor is it practicable to issue new securities with a lien limited to the property that was covered by the old lien. There must be segregation of the system earnings to each existing lien and allocation of securities representing the system value to each class of claimants. This was done here as shown in the second table in note 6.[23] Such a method is in full accord with the principle

[19] 318 U. S. at 482 and 483; 318 U. S. at 539-541.

[20] Ecker v. Western Pacific R. Corp., 318 U. S. at 475-76.

[21] 233 I. C. C. 578-81.

[22] 254 I. C. C. at 359.

[23] See for discussion of the formulae 233 I. C. C. at 581 *et seq.*; 254 I. C. C. at 16 and 359-76.

that senior creditors are to retain their relative priority of position in a reorganization. *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. at 561-64. Furthermore, junior claims can receive nothing until the senior claims receive securities of a worth or value equal to their indebtedness. 318 U. S. at 483; 318 U. S. at 569. The Generals are definitely junior. 223 I. C. C. at 524.

The Commission did not make a finding that the cash value of the securities awarded the senior claimants as of the effective date of the plan equalled the face of the claims. It did, however, carefully state its reasons for concluding that the compensation "flowing under the plan to the various classes of bondholders for the rights surrendered by them" was adequate in the light of the full priority rule. 254 I. C. C. at 360. For those classes, other than the Junior Generals, that received common stock, the Commission said that the possibility of "unlimited dividends on common stock" was a factor in offsetting loss of position.[24] Thus it is clear that when the Commission made its allocations it had definitely in mind that one thing that gave the senior creditors compensation for the admission of junior claimants to participation in securities before the seniors obtained full cash payment was their chance to share in the unlimited dividends that might be earned and paid on the common stock to have a part in the "lush years." It should be noted that income applicable to dividends was at its highest in 1942 prior to the approval of the plan by the Commission in June, 1943. Therefore the abnormal earnings of 1942 were in the Commission's contemplation when it spoke of the opportunities for "unlimited dividends." Its discussion of the plan assumed that 1943 available earnings might be as large. 354 I. C. C. at 355.

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[24] Rio Grande Western consolidated, 254 I. C. C. at 365: "Loss in earnings position and surrender of other rights, in our opinion, are offset by the possibility of increased return permitted by the 4½ percent income bonds, 5 percent convertible preferred stock, unlimited dividends on common stock, and the other features of the plan."

Denver & Rio Grande consolidated, *id.* at 364: "This apparent change in earnings position is offset by the new sinking fund and capital fund and by the increased rate of return obtainable from the new securities, i. e., slightly in excess of 4.5 percent for 64 percent of the claim and unlimited stock dividends for the remainder."

Denver & Rio Grande Western refunding and improvement, *id.* at 366: "They also will receive whatever dividends may be paid on 97,706 shares of common stock."

The improved physical condition of the road through expenditures of the trustees for previously deferred maintenance, improvements and new equipment was before the Commission and necessarily entered into their valuation of the property. 233 I. C. C. 531.

There is another important factor, corollary to stock ownership, to be noted in the Commission's allocation of these securities. This factor is that the creditors who received common stock to make them whole obtained with that common stock an interest in all cash on hand or all cash that might be accumulated. Of course, the Commission thoroughly understood this. In fact, it referred to the ten million plus of cash on hand as of January 1, 1943. 254 I. C. C. 353. Immediately following this reference is a full discussion of the cash needs of the road for the year 1943, including additions, betterments and new equipment, and the amount which it was estimated would be in the treasury at the end of the year. That was $15,600,000. This cash would be reflected in the value of the common stock. The petitioner states that the highest when-issued Stock Exchange price in 1945 for the common stock was $31½, par $100. See Commercial and Financial Chronicle, May 13, 1946, p. 2618, where the common is quoted at 29 Bid, 31 Asked. Cash, material and supplies, as well as all other assets and all liabilities of the debtor were represented by the securities. If there is more cash on hand than needed, for taxes, expenses and proper improvements, it is at the disposal of the common stockholders. If money was used to pay indebtedness, there would be a corresponding reduction in the capital structure. Therefore, the plan provided, 254 I. C. C. at 386:

> "The new company shall be deemed to have come into possession of the properties as of the effective date of the plan.
>
> . . . The capitalization of the new company, as of January 1, 1943, after consummation of the plan . . . shall consist substantially of the following securities, excluding those to be pledged, the amounts stated being subject to reduction to the extent, if any, that matured interest proposed to be funded in the plan is paid, and as equipment obligations or other liabilities are paid or reduced . . . ."

It is accepted by the senior claimants that the plan is fair and equitable as between themselves. If our conclusion that the method and result of valuation is sound, the allocation of ten per cent of

their claim in common stock to the Generals follows as a matter of computation.

It would also follow that the objection of a stockholder, the Missouri Pacific Railroad Company, through its Trustee in reorganization, to a voting trust for future control of the debtor would be ineffective because this stockholder is eliminated from the reorganization by the valuation of the property and allocation of securities. For the Commission's reasons for creating a voting trust see 233 I. C. C. at 581, 254 I. C. C. at 33, 35, 367.

Cash and War Earnings. The Circuit Court of Appeals was of the view that war earnings were of "very little value in estimating the probable future earnings of this property in the peace economy which is to come" and that the Commission was well within its right in appraising them lightly. 150 F. 2d at 34. This was after the seventeen million earnings of the top year 1942. The appellate court agreed, too, that excess current assets should not be capitalized and that improvements made during the trusteeship for reorganization had been considered by the Commission and District Court in fixing their valuation by past and prospective earnings. 150 F. 2d at 35. The appellate court then made the following ruling:

> "The Senior Bondholders were paid in full. They received all the new securities and most of the common stock. Ninety per cent of the General Bondholders' claims were wiped out. They received only a small amount of common stock, ten per cent of their total claim. Adequate operating funds are essential to the operation of a railroad. The Senior Bondholders were entitled to receive in addition to the full amount of their claims, working capital sufficient for proper and efficient operation of the railroad. But anything in excess of what was reasonably necessary for this purpose constituted assets of the insolvent corporation which belonged to the remaining creditors.
>
> "We think it is apparent from the record that there were current assets on hand consisting of cash and securities in excess of what was needed for the efficient operation of the road. As pointed out, the working capital of the debtor had increased from a deficit of $9,727,230 as of December 31, 1935, to a surplus of $12,125,863.50 as of December 31, 1944. While these increased net earnings are due in large part to the war and will not continue after the end of the war, and may therefore be disregarded in setting up the capitalized structure based upon prospective earnings, we cannot disregard the fact

that these huge surpluses actually exist. Their existence is an accomplished fact. It is also obvious that surpluses will continue to pile up for a reasonable time yet to come. We think any plan which fails to take this into account and which gives the Senior Bondholders their claims in full by substantially delivering the road to them, and gives them the surplus cash actually on hand and further enables them to receive in addition the excess war profits which are reasonably sure to come, is inherently inequitable and unfair, so long as there are classes of creditors whose claims are not fully satisfied."

In our judgment this holding is erroneous.

The effective date of the plan was fixed by the Commission as January 1, 1943. This was in its power.[25] The allocation of the securities took into consideration the interest of the secured claims to that date. Any gain or any loss after that time was a benefit or an injury to the new common stockholders and then sometimes to security holders in positions senior to them. Assuming that the courts, as courts with equity powers in a bankruptcy matter, might set aside a plan, fair and equitable when adopted by the Commission, merely on account of subsequent changes in economic conditions of the region or the nation,[26] it should not be done when the changes are of the kind that were envisaged and considered by the Commission in its deliberations upon or explanations of the plan.

We have poiated out in the section of this opinion dealing with the allocations of the securities that a part of the compensation to senior claimants for their loss of position was the opportunity to participate in war earnings. This was understood by the District Court[27] and the Commission.[28] Accumulations of cash beyond operating fund needs are in the same category. In dealing with the problem the Commission noted that a five percent divi-

[25] Ecker v. Western Pacific R. Corp., 318 U. S. at 509.
Interest accrues on the secured claims until the effective date of the plan. Group of Investors v. Milwaukee R. Co., 318 U. S. at 546. Compare Ticonic Bank v. Sprague, 303 U. S. 406.

[26] 318 U. S. 506-509.

[27] 62 F. Supp. at 390:
"The $25,000,000 or more the Trustees have expended in the Improvement Program inures to the benefit of the common stock. If the latter is worth anything it is as much due to these expenditures as to any other factor. This, with the increase in current assets and wartime earnings which counsel seem to believe are permanent, constitute the only equity behind the preferred and common stock."

[28] 254 I. C. C. at 356.

dend on the authorized common would require an income available for interest and dividends of $7,969,629. The Trustee for General bonds claims no such earnings between 1929 and 1942. Even before the transportation difficulties of 1946, it was obvious that the Commission's judgment was being confirmed by events. See note 18, *supra*.[29]

The error of the Circuit Court in its holding set out above lies in its assumption that the senior bondholders were paid in full by the securities allotted to them without also accepting the determination of the Commission that the assets represented as of January 1, 1943, and all subsequent earnings were a part also of the common stock that was awarded the senior bondholders.

Decreases in Senior Debt. The plan provides for securities to take the place of the Rio Grande Junction's first 5's in the face amount of $2,758,333 and for the assumption by the reorganized road of $5,758,000 equipment obligations. All of these securities are senior to the Generals. The Denver purchased the Junctions and paid $1,218,000 on the Equipments. This reduced the necessary capitalization by that aggregate sum. The Circuit Court of Appeals was of the opinion that "The value behind these securities in no wise belonged to the Senior Bondholders, because they had been paid in full". 150 F. 2d 39. This ruling, we conclude, was erroneous for the same basic reason that we held the cash and war earnings belong to the owners of the common stock.

We called attention, *supra* page 16, to the authority granted the District Court to reduce the capitalization of the new company as interest due on January 1, 1943, or equipment obligations or other liabilities were paid. The District Court acted on this authority and in its approval of the plan said of the Junctions, "They may be canceled or they may be utilized under the plan in

[29] Mankind's foresight is limited. The uncertainties of future estimates are recognized. It is not without interest to note, however, that on April 15, 1946, the railroads of the United States petitioned the Interstate Commerce Commission for increased freight rates and charges. This was said:

"The situation of the railroads has now become critical and their need for a substantially higher level of freight rates has become imperative. This is the result of an extraordinary combination of war and postwar conditions with which the railroads are confronted, and more particularly the result of three factors of recent development: (1) the increase in wages of railroad employes of 16 cents per hour determined under the procedures of the Railway Labor Act in April, 1946, retroactive to January 1, 1946; (2) large increases, both present and prospective, in the prices of railway materials and supplies;

acquisition of new securities which will become an asset of the reorganized company." C. C. H., Bankruptcy Law Service Decisions 1942-1945, ¶ 54,562 at p. 55,635. The Junction bondholders did not vote on the plan. Under our determination that the creditors who received common stock were compensated partly by the assets and future earnings, it is obvious that the use of such assets to retire senior claims is a part of the normal and expected increment from holdings of common stock. The increase of common stock by the Commission to the Generals from five to ten per cent of the bondholders' claims, preliminary to the adoption of the plan, 254 I. C. C. at 352, 359, is partly attributable to a reduction of necessary capitalization. This increase in junior participation differs from that now proposed. The former reduction of senior capitalization could be carried out because earnings prior to the adoption of the plan made it unnecessary to borrow money for reorganization. When proposed capitalization is being planned on earnings, a reduction of senior capital without reduction of estimated earnings increases possible junior capital within the scheme. When the reduction of senior capital takes place after the adoption of the plan by use

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and (3) a sharp decline in volume of railway traffic and an even greater decline in railway revenue.

"The volume of freight and passenger traffic is falling continuously, and it is anticipated that the downward rate will accelerate in the months to come. The revenues will be reduced by reason both of the decline in volume and a return to a more nearly normal composition of traffic. It is estimated that the operating revenues of Class I railroads for 1946, on the basis of the present rates, fares and charges, would be approximately $6,800,000,000, or 23.5 per cent less than they were in 1945.

"Freight and passenger traffic reached their peaks in 1944. But net railway operating income and net income began to diminish in 1943 on account of rising costs of operation. In the face of increasing traffic through 1944, both net railway operating income and net income moved steadily downward after reaching their peak in 1942. With the cessation of hostilities in 1945 there began to be a decline also in gross revenues which is expected to become more pronounced as the abnormal war conditions disappear, disabilities of highway carriers and other agencies of transportation are removed, and the prewar pattern of railway traffic is resumed."

The Denver apparently did not vary greatly from this overall picture. Its net revenue for 1945 from railway operations dropped from $20,569,809 to $14,246,504. Its gross operating revenue, however, increased four and a half million. The loss in net was due largely to increased amortization of defense projects.

The monthly report of revenues and expenses by the Denver for January and February of 1946 shows a decrease of operating revenues from $10,856,764 to $8,932,983.

of anticipated earnings or existing cash, there can be no such readjustment of junior participation because assets in the balance sheet at the adoption of the plan and subsequent earnings are, as we have pointed out, for the benefit of the stockholders in the new company so that through these common stock advantages these new stockholders may be compensated for their loss of payment in full in cash. Of course, this section of the opinion is written and must be read on the assumption that the allocations of common stock are fair and equitable, a matter discussed *supra*.

Utah Fuel Company Stock. The Rio Grande Western Railroad Co. in 1899 executed its First Consolidated Mortgage, an indenture to secure its issue of First Consolidated Bonds, maturing April 1, 1949. Rio Grande Western reserved the right to issue additional bonds under the indenture.

The Utah Fuel Company was organized in 1900, with a capitalization of 100,000 shares. In 1901 an agreement was entered into by Rio Grande Western, the trustee under the First Consolidated Mortgage, and the owner of the Utah Fuel stock. The contract provided that the stock would be held by the trustee to secure bonds issued under the First Consolidated Mortgage and that Rio Grande Western would have the right at any time on paying the trustee $6,000,000 in cash or delivering an equal face amount in First Consolidated bonds to receive the Utah Fuel stock, free of the mortgage lien. Subject to the lien, the stock was transferred to Rio Grande Western. $6,000,000 in additional First Consolidateds were issued to the owner of the stock.

In 1908, the Denver & Rio Grande Railroad Company was organized and acquired the property of Rio Grande Western, assuming the obligation of its First Consolidated Mortgage bonds of 1899. The equity of redemption of Denver & Rio Grande Railroad Company in the Utah Fuel stock was sold in 1918 under execution and transferred to the Western Pacific Railroad Corporation.

In 1924 under an agreement among the Denver & Rio Grande Western Railroad Company, the Western Pacific Railroad Corporation, Missouri Pacific Railroad Company, and T. S. Alexander, who by the agreement became trustee of the equity of redemption in the Utah Fuel stock, Western Pacific transferred to T. S. Alexander, Trustee, subject to the pledge under the Consolidated Mortgage its Utah Fuel stock and the debtor transferred

to said trustee whatever interest it had in the stock, through certain releases, not here important.

The agreement first provided that the ultimate beneficial interest in the Utah Fuel stock so held was vested one-half in Missouri Pacific and one-half in Western Pacific. Except for certain contingencies not here important, it was provided that the trustee under the 1924 agreement would pay all dividends received by him from the trustee under the Consolidated Mortgage on Utah Fuel stock to the debtor so long as any of the General or Refunding bonds were outstanding.

The agreement further provided that if the General Mortgage or the Refunding or other mortgage of the debtor were foreclosed, the trustee would sell the interest of these mortgages in the Utah Fuel stock subject to the Consolidated Mortgage, if outstanding, and apply the proceeds to the payment of the bonds secured by the equity of redemption in the stock dividing any surplus between Western Pacific and Missouri Pacific.

The General Mortgage and Refunding bonds created in the 1924 reorganization were thus given a lien on the Utah Fuel stock, junior to the lien of the Denver & Rio Grande First Consolidated Mortgage.

Under the plan approved by the Commission and the District Court, the First Consolidated bonds were allotted 20% of their claim in new income bonds, 73% in preferred stock, and 7% in common stock. The plan further provided, 254 I. C. C. at 398-99, that:

> "The trustee under the Rio Grande Western Railway Company consolidated mortgage shall be permitted to obtain the release of the equities in the stock of the Utah Fuel Company and distribute the stock among the holders of the aforesaid bonds in any manner agreeable to them, or to enforce its rights as pledgee of the stock of the Utah Fuel Company, the proceeds recovered to be distributed to the holders of the bonds."

The Commission took the position that this and the other features of the treatment of the First Consolidated bonds were justified as compensation for "loss of earnings position and surrender of other rights"[30] under the plan.

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[30] See note 24.

The Commission made no definite finding with respect to the value of the Fuel Company stock. The Commission had before it evidence through 1936 with respect to the value of the stock as well as an appraisal of the value of the Fuel Company made for the trustee of the First Consolidated Mortgage, which indicated a value of $4,653,720. The only dividend paid to the debtor by Utah Fuel under the 1924 agreement was in 1934 and amounted to $250,000; the debtor in applying its formula for allocation of earnings by mortgage districts credited the Consolidated Mortgage with an income of $83,333 per annum based on that dividend payment allocated over the three-year period, 1932 to 1934. The status of the stock was considered by the Commission in its original report and its several supplemental reports, and its proposals with respect to the stock remained unchanged.

In proceedings before the District Court in 1943 on objections to the plan, it was revealed that the Fuel Company's net income for 1942 was $415,000 and for the first seven months of 1943, $535,869.[31] The company has no funded debt.

In the Circuit Court the respondents contended that the holders of the First Consolidated bonds should be compelled either to foreclose this collateral, applying the proceeds to their claim, or credit their claim with the value of the collateral and be allowed new securities only for the balance. The Circuit Court disapproved the treatment by the plan of the General bondholders with respect to the Fuel Company stock pointing to the fact that the Commission had permitted "doubts and uncertainties" to remain with respect to the value of the collateral, and that there was a danger that if the collateral had substantial value, the First Consolidated bondholders might receive more than full payment.

The facts set out above fully support the conclusion of the Commission that the "title to the stock is vested in the Missouri Pacific and Western Pacific." Whatever rights the debtor may have retained after the sale of the stock on execution in 1918 were released to the trustee and the two railroads in 1924. We have then a situation in which the holders of the ultimate beneficial

[31] According to Moody's Manual the net income of the Fuel Company for 1943 was $865,140, 1944 $653,901, and earned surplus at the end of the latter year $4,862,980.

interest in stock which had been pledged previously under a mortgage have permitted that interest to be encumbered by a third person, namely the debtor, as security for its General and Refunding bonds. The rule is settled in bankruptcy proceedings that a creditor secured by the property of others need not deduct the value of that collateral or its proceeds in proving his debt. *Ivanhoe Bldg. Loan Assn. v. Orr*, 295 U. S. 243. We see no reason why the same should not be true under § 77. See *New York Trust Co. v. Palmer*, 101 F. 2d 1, 3. Therefore the First Consolidated Mortgage bonds were properly permitted to prove the full amount of their debt.

Respondents, speaking only for the General bondholders, object that the plan gives the First Consolidated bondholders all the Utah Fuel stock or its proceeds in addition to securities the face value of which amounts to one hundred per cent of their claims. The Refunding bondholders make no objection. It is thus contended that the plan deprives the General bondholders of their junior interest in the stock without a determination of the value of that stock, or a finding of the extent to which the Consolidated bondholders have been paid by the new securities to be given them. We do not so read the plan. The plan provides merely that the trustee of the Consolidated Mortgage "shall be permitted to obtain the release of the equities in the stock of the Utah Fuel Company" and distribute the stock or its proceeds to the holders of the bonds. This statement contains at least two requirements to be met before the Consolidated bonds obtain anything from the collateral. The first is that the trustee of the First Consolidated Mortgage be in existence. Even after the plan goes into operation and the old securities are surrendered for cancellation there is no requirement that the trusts terminate since they will continue to hold property other than that of the debtor. Section 77(f), which deals with the effect of a confirmation and the discharge of the debtor from liability, does not so require. Hence whatever action the trustee of the Consolidated takes may be commenced prior to or after the consummation of the plan. This will permit the respondent trustee under the General Mortgage, which would continue in existence for the purpose, to take the necessary steps to safeguard its rights in the collateral on behalf of the Generals.[32]

[32] Obviously, the Fuel stock or its proceeds could be distributed to record holders of the old securities as of the date or dates of distribution of the new securities.

The second requirement, which is explicit in the plan, is that the trustee obtain the release of the equities in the stock. The junior lienors have an absolute right under the terms of the 1901 pledge and the 1924 agreement to all the proceeds of the stock over $6,000,000 and a right also to any part of the proceeds not needed to make the First Consolidated bonds whole. The trustee of the Consolidated concedes in its brief here that enforcement of the pledge "can be brought about only through judicial proceedings." It correctly points out that in such proceedings full protection can be given to all those who have any junior interest in the stock. Respondents' fear that the General bondholders and the mortgage trustees for the junior interests will not be in existence and so unable to protect themselves has been above demonstrated to be without foundation in fact.

The result is that this feature of the plan did not in any way change or affect existing rights in the collateral. The respondents may show in the judicial proceedings which must be brought by the trustee of the First Consolidated Mortgage that the First Consolidated bonds have been fully paid by the securities awarded them under the plan, if such be the fact; or the respondent, trustee of the General, may itself bring a proceeding against the trustee of the First Consolidated mortgage for a determination of the rights of the Generals. Petitioners concede, as they must, that they are not entitled to more than full payment and that they are under a duty to account to the respondents for any surplus remaining after they have been made whole.[33]

The treatment of the Utah Fuel stock in the plan is consistent with the Commission's disposition of certain collateral pledged with the Reconstruction Finance Corporation and the Railroad Credit Corporation by parties other than the debtor to secure notes of the debtor in the *Western Pacific* case. *Western Pac. R. Co. Reorganization*, 233 I. C. C. 409, 432. The Commis-

[33] There is a certain illogic in the position of First Consolidated bonds in asserting any rights in the collateral at all. If, as they concede and we now hold, they are entitled to be paid in full in new securities without regard to the collateral, it may be that they have been fully paid by the new securities given them since they do not complain of their treatment under the plan. Since they are entitled only to full payment it would then seem to follow that they have no rights against the collateral. We should not be taken as deciding this question, however, since we leave it to an independent suit in which there is jurisdiction over the proper parties.

sion permitted the pledgees to retain the collateral and this Court approved that action, saying, "This collateral, other than the refunding bonds, was therefore left with the pledgees with its position unaffected by any direct action of the Commission." *Ecker* v. *Western Pacific R. Corp.*, *supra*, at 506.

Reasonableness of Rejection. As the conclusions of the Circuit Court of Appeals upon the allocation of securities, the treatment by the Commission of cash, war earnings, and decrease in debt with priority over the Generals differed from those made by this Court, that court's conclusion that the General bondholders were reasonably justified in rejecting the plan followed naturally. 150 F. 2d 40. Section (e) gives power to a class, here the General bondholders, to reject the plan subject to the power of the District Court, after certification of the result of the submission, to "confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e)." 11 U. S. C. § 205; see note 9, *supra*.[34] The plan was confirmed after appropriate findings. 62 F. Supp. at 390.

This provision for confirmation of a plan despite rejection by a class appeared in the draft for the 1935 amendments. Apparently it caused no particular comment.[35] We think that the provisions

[34] Clauses (2) to (3) are not involved. They relate to expenses, fees and costs.

[35] H. Rep. No. 1283, 74th Cong., 1st Sess., p. 18. S. Rep. No. 1336, 74th Cong., 1st Sess., p. 3, contains the following statement: "Further, the consent of two-thirds of each class of stockholders must be acquired, unless, by an elaborate valuation proceeding, it is proved that the value of the property is so low that the stock has no interest. This is an effective obstruction. . . .

"In order to remedy these defects, S. 1634, as amended, provides that two-thirds of those of each class who vote upon a plan will bind the dissenters or those failing to vote. But it also provides that the court may make effective a fair plan where the parties do not agree. . . . If two-thirds of each class consent, the plan will bind the remainder of each class. But the judge may make the plan effective, even if not so accepted, if he finds that it conforms to the requirements just stated, provides fair and equitable treatment for the interests of those rejecting it, and that their rejection is not reasonably justified in the light of the respective rights and interests. These provisions give complete due process of law from a procedural standpoint, there being provision for full hearings both before the commission and the court. Within the broad powers of Congress under the bankruptcy clause as recently declared

for confirmation by the courts over the creditors' objection are within the bankruptcy powers of Congress. Those powers are adequate to eliminate claims by administrative valuations with judicial review and they are adequate to require creditors to acquiesce in a fair adjustment of their claims, so long as the creditor gets all the value of his lien and his share of any free assets.[36]

The grounds accepted by us in former sections of this opinion as sustaining, as of January 1, 1943, the valuation of the road, the allocation of the securities, and the treatment of cash, war earnings and capital reductions, establish that for the act of confirmation on November 29, 1944, over the objection of the General bondholders, the finding of the judge that the plan then made "adequate provision for fair and equitable treatment" of the dissenters was justified. 62 F. Supp. at 390. In view of the District judge's familiarity with the reorganization, this finding has especial weight with us. See Rule 52 F. R. C. P. There is no doubt that the plan then conformed to subsection (b) and the other requirements of the first paragraph of subsection (e). Note 9 *supra*.

This leaves for consideration the question of whether, the plan being fair and equitable as of June, 1943, effective January 1, 1943, the Generals were reasonably justified in rejecting the plan by ballots cast between April 26 and July 15, 1944.

As we have pointed out under *Allocation of Securities, supra*, the Commission's plan was adopted after 1942, the year of greatest profit and with anticipation on the part of the Commission that there might be other "big" years but with realization that the war profits were not a sound basis for higher valuation. Current reports of earnings were a part of the record. Nothing that respondents have called to our attention indicates any improvement in economic conditions or prospects in July, 1944, or any date since, over June, 1943, the date of the Commission's approval of the plan, which would justify a treatment different from that ac-

by the Supreme Court in Continental Illinois Bank & Trust Co. v. Chicago, Rock Island & Pacific Ry. Co. (55 Sup. Ct. Rep. 595), the provisions also afford due process of law in fully protecting the property rights which are involved."

See also Hearings, House Judiciary Committee, 74th Cong., 1st Sess., on H. R. 6249, Serial 3, pp. 15 and 22.

[36] Wright v. Union Central Ins. Co., 311 U. S. at 278, and discussion at pp. 8 and 9, *supra*.

corded the claimants in 1943.[37] The challenge to the reasonableness or the unreasonableness of the rejection of the plan is not based on any change of conditions since its approval by the District Court October 25, 1943. Under subsection (e), note 9 *supra*, the judge automatically confirms a plan after a vote of classes of creditors if satisfied that two-thirds of each class have accepted. If there is a rejection, there is a reexamination of the plan to assure that those who dissent have had fair and equitable treatment. Apparently the reexamination for this treatment does not differ from that for the original court approval under the first paragraph of subsection (e). It does, however, center upon the rights of those who rejected the plan.

A rejection would not be reasonably justified unless the dissenters had a valid reason for their vote. As is shown by Judge Symes' discussion of their objections to confirmation,[38] their reasons were the payment of the senior obligations with consequent claimed release of capitalization for junior securities and the inadequate valuation, particularly in view of the large additions to plants from earnings. We think that we have demonstrated that there was an adequate basis for the valuation, see page 10 *et seq.*, and that the decreases in senior debt were not for the account of the junior creditors. See pp. 19-20, *supra*. Respondents offer no other ground for their votes in rejection.

Congress with its purpose to stop the blockade of sound reorganization by classes of creditors with the veto power of the 1933 statute, note 35, *supra*, certainly did not intend to leave a class with the same power of interference because in its reasonable judgment that class thought the valuation was erroneous or the senior creditors were paid in full by the face value of securities. If a plan gives fair and equitable treatment to dissenters, the elements which make the plan fair and equitable cannot be the basis for a reasonably justified rejection. If only those elements are relied upon, as here, the rejection is not reasonably justified.

Of course, this does not mean that if a plan is approved as fair and equitable by the Commission and court, there cannot be a reasonable justification for its rejection by a class of claimants on submission. Reasons to make their rejection reasonable may

[37] Cf. I. C. C. v. Jersey City, 322 U. S. 503, 515.
[38] 62 F. Supp. 384.

arise thereafter. For example, unanticipated, large earnings might develop. We see no reasonable justification here for the action of the General bondholders.

In conclusion, we shall add that the foregoing opinion has been written without heavy reliance upon the duty of the Commission to plan reorganizations with an eye to the public interest as well as the private welfare of creditors and stockholders.[39] The Commission had this duty in mind. Our failure to comment more upon that feature of the plan should not be interpreted as an intimation upon our part that it is not important. These respondents cannot be called upon to sacrifice their property so that a depression-proof railroad system might be created. But they invested their capital in a public utility that does owe an obligation to the public. The Insurance Group Committee, with fiduciary responsibility to the myriad holders of policies, and the other investors or speculators in senior bonds as well as the holders of General bonds or other investors or speculators in junior security issues, by their entry into a railroad enterprise assumed the risk that in any depression or any reorganization the interests of the public would be considered as well as theirs. That public interest in an efficient transportation system justifies the Commission's requirements for reasonable maintenance and improvement of the properties and for a capitalization with fair prospects for dividends on all classes of securities.[40]

The judgment of the Circuit Court of Appeals is reversed and the orders of the District Court of October 25, 1943, approving the plan, and of November 29, 1944, confirming the plan, are affirmed.

The cause is remanded to the District Court for further proceedings.

It is so ordered.

Mr. Justice FRANKFURTER dissents, and will set forth the detailed grounds for his dissent in an opinion to be filed hereafter.

Mr. Justice JACKSON took no part in the consideration or decision of these cases.

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[39] § 77(d), note 9, *supra*. 318 U. S. at 473; 318 U. S. at 544.

[40] See concurrence of Commissioner Eastman, Western Pac. R. Co. Reorganization, 233 I. C. C. at 437.

SUPREME COURT OF THE UNITED STATES

Nos. 278, 279, 280, 281 and 282.—October Term, 1945.

Reconstruction Finance Corporation; Insurance Group Committee; Guaranty Trust Company of New York, Trustee, Rio Grande Western Railroad Company Consolidated Mortgage; Central Hanover Bank and Trust Company, Trustee, Rio Grande Western Railroad Company First Trust Mortgage; United States Trust Company of New York, Trustee, Denver and Rio Grande Railroad Company Consolidated Mortgage; and The Chase National Bank of the City of New York, Trustee, Denver and Rio Grande Western Railroad Company Refunding and Improvement Mortgage, Petitioners,

278 v.

The Denver and Rio Grande Western Railroad Company, et al.

Same,

279 v.

The Denver and Salt Lake Western Railroad Company, et al.

Same,

280 v.

City Bank Farmers Trust Company, Trustee Under the Debtor's General Mortgage.

Same,

281 v.

The Denver and Rio Grande Western Railroad Company, et al.

Same,

282 v.

Guy A. Thompson, Trustee, Missouri Pacific Railroad Company, Debtor.

On Writs of Certiorari to the United States Circuit Court of Appeals for the Tenth Circuit.

[October 28, 1946.]

MR. JUSTICE FRANKFURTER, dissenting.

On November 1, 1935, The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company (hereinafter compendiously called "the debtor"), initiated these proceedings for their reorganization under § 77 of the Bankruptcy Act, 47 Stat. 911 (1935), 11 U. S. C. § 205. The plan of reorganization here in controversy was approved by the Interstate Commerce Commission on June 14, 1943. 254 I. C. C. 349, 385. The District Court approved the plan for necessary submission to the various classes of creditors. C. C. H. Bankruptcy Law Service ¶54, 562. All classes except the holders of the general mortgage bonds accepted the plan. On the effective date of the plan, the claims of these General Bondholders constituted about one-fourth of the debtor's entire debt. Just short of eighty percent of this class of creditors (79.33%) voted to reject the plan. Congress has made the right of any class to reject a plan subject to the power of a district court to override such rejection, if the judge "is satisfied and finds * * *" that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts." 47 Stat. 911, 919 (1935), 11 U. S. C. § 205 (e). The District Court on November 1, 1944, found that all the requirements of the statute had been met, and confirmed the plan. 62 F. Supp. 384. But the Circuit Court of Appeals for the Tenth Circuit, a strong bench, on May 10, 1945, found that "the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, and that the District Court was without authority to confirm the plan in the face of their adverse vote." 150 F. 2d 28, 40. On a fair construction of the requirements of Congress for the adjudication of railroad reorganizations, as applied to the situation before us, I cannot escape agreement with the Circuit Court of Appeals.

Railroad reorganizations are so enshrouded in the confusing intricacies of high finance that the true nature of decisive issues is too often lost to view. It may be useful to an appreciation of what appears to me to be the crux of the case to put a situation that is sufficiently analogous but much more familiar. In the early depression years the big life insurance companies foreclosed a large number of farms. The foreclosure process, we assume, involved the control of the farm and all its income by a judge. The hypothetical farm began to make a fair income, enough to pay the insurance company a considerable part, if not the whole, of the annual interest. But instead of paying the interest, the judge applied the money to rebuild the homestead, to add a new barn, to purchase an adjacent field, the most modern machinery and additional head of cattle. Thereby the farm became far more valuable than at any time since the insurance company placed the mortgage on it. Moreover, the judge retained as cash in the bank a portion of the income sufficient to pay off at least twenty percent of the mortgage. The farmer thinks he ought to be allowed to use the cash to reduce the mortgage, should be given credit for the income which the judge used to make the considerable improvements and which could have been used to reduce the mortgage. This would appear to be a natural attitude on the part of the farmer, and it would hardly seem that he was not reasonably justified to resist the claim of the insurance company to the farm, with all its improvements as well as the cash in bank.

This simple analogy may look almost trifling alongside the complicated details involved in a plan for the reorganization of a railroad system. But is it an oversimplification of the controlling issue, namely, was the Circuit Court of Appeals wrong in holding that the General Bondholders were "reasonably justified" in rejecting the plan? Let the facts, clearly and fairly stated in the opinions below, speak for themselves. Judge Huxman thus sum-

marizes the Court's conclusion that the General Bondholders had "a real grievance":

> "On November 1, 1935, the Debtor's total debts senior to the claim of the General Bondholders was slightly over $101,000,000. The General Bondholders' claims at that time were approximately $30,000,000, making the total of the two claims approximately $131,000,000. Any one of the ten plans of reorganization prior to the final one fixed the value of the property at more than enough to satisfy the claims of all bondholders in full, as of the date this proceeding was instituted. During the ten intervening years, the claim of the Senior Bondholders increased to more than $139,000,000, and that of the General Bondholders to more than $43,500,000, making a total of more than $182,000,000, required for the two classes of claims.
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> During all of this period the Debtor enjoyed substantial income, amounting to approximately $50,000,000. Instead of using this income in payment of interest on the senior claims, it was used in making permanent and lasting improvements in the road. More than $43,000,000 was used in this way. None of these expenditures has resulted in a comparable increase or in any substantial increase in the final valuation, over the valuation prior to the making of the improvements. But as a result of this operation, the position of the General Bondholders has deteriorated from a 100 per cent participation in the amount of their claims to a mere ten per cent. Nor does it change the picture to say that these improvements were necessary to the railroad system. The fact still remains that earnings in which all had a vital interest were used in building a new railroad in many respects, which will be handed over to the Senior Bondholders, and the General Bondholders will practically be eliminated as a result thereof.

But this alone does not entitle the General Bondholders to a greater participation in the reorganized company. Neither does it condemn the plan of reorganization or the capital structure set up therein. The operation of a railroad involves the expenditure of large sums for operation. It involves the formulation of plans of operation and the exercise of judgment and discretion. If, in the exercise of this discretion, funds are unwisely spent, from the viewpoint of the interest of all creditors, they may feel aggrieved, but they have no legal cause of complaint.

Neither was the Commission compelled to, nor would it be justified in adding the amount of these expenditures to the capitalized value if in the exercise of sound discretion it felt that the reasonable prospective earnings of the road, after the improvements did not justify it. However, in the face of all this, after satisfying in full the claims of the senior bondholders, the plan of reorganization should have made sure that all excess current assets, as well as all excess war profits yet to accrue, would go to the General Bondholders.

The commission, as pointed out, adopted a conservative, sound estimate of the prospective earnings of the reorganized company. For this it is not to be criticized. An over-optimistic view would again surely lead the Debtor into the bankruptcy courts, with which it has had too much acquaintance already.[7] We, however, feel that there is more than a

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[7] "Properties included in this railroad system have participated in the following reorganizations: The Denver & Rio Grande R. Co. was a successor in a reorganization proceeding in 1886; the Rio Grande & Western R. Co. was the successor in a reorganization proceeding in 1889; these two companies consolidated in 1908 under the name of the Denver & Rio Grande R. Co.; the present company was reorganized in 1920 and again in 1922 to 1924.".

speculative probability that these war industries which have been constructed along the system, as well as the improvements which have been made by the use of these net earnings, might produce greater net returns than anticipated in the plan. If such should be the case, they certainly belong to the General Bondholders and not to the Seniors, and the plan should bring this about. It could be done by issuing to the General Bondholders an additional amount of a subordinate stock which would receive returns only from excess dividends. This is a mere suggestion on our part, and in no wise binding on the Commission. Our duty is limited to pointing out defects in the plan. It is the responsibility of the Commission to correct them.

The Junction Bonds

We think that the complaint as to the manner in which the Junction Bonds were handled is well taken. The Rio Grande Junction Railroad is a wholly owned subsidiary of the Debtor. It had bonds outstanding in the hands of the public for the payment of which the Debtor was liable, totaling $2,758,333. This claim was senior to that of the General Bondholders. The plan set aside securities for the payment of this claim. In an order dated September 13, 1943, the District Court directed the trustee to pay this claim with some of the surplus cash on hand, and retained the securities which were to be used in the payment thereof in the treasury of the company. The court treated the transaction as a purchase of securities rather than a payment of a debt. This is a play upon words; and, in any event, is immaterial to the issue. The fact remains that the new capitalization provided securities for the payment of these bonds. The value behind these securities in no wise belonged to the Senior Bondholders, because they had

been paid in full. When surplus cash was used to pay this claim, the value behind the securities set aside for that purpose remained undistributed. Since the Senior Bondholders had been satisfied in full, this undistributed value in all equity and fairness belonged to the General Bondholders. Any plan which does not give it to them does not comply with the requirements of Section 77, sub. e, of the Act." 150 F. 2d 28, 38–39.

Inasmuch as the decision in this case seems to me to turn on an adequate appreciation of the facts, I deem it important to quote the analysis of the situation on the basis of which Judge Phillips reached his conclusion:

"On November 1, 1935, during the depths of the national depression, the debtor came into court for reorganization. At that time the debtor's senior debts ahead of the general mortgage bonds aggregated slightly over $101,000,000 and the claim of the general mortgage bondholders aggregated about $30,000,000. With an immediate reorganization, a capitalization of $132,000,000 would have been adequate to give the general mortgage bondholders new stock equal to 100 per cent of their claim. No capitalization or valuation ever proposed for the debtor, in any plan presented, has been that low. During the eight years' delay in reorganization (in nowise due to the general mortgage bondholders, but, at least in part, to controversies among the senior security holders) and up to January 1, 1943, the effective date of the plan, the claims of the senior security holders, due to the accrual and nonpayment of interest, increased about $38,000,000. The debtor's net income available for interest during the trusteeship to the end of 1944 amounted to $49,420,972. It exceeded by approximately $9,500,000 the interest charges which accrued on the claims of senior security holders to

the end of that year. As of December 31, 1935, the debtor's current assets were $9,727,230 less than its current liabilities. As of December 31, 1944, the debtor's current assets exceeded its current liabilities by $12,125,863.50. Thus, it will be seen there has been a favorable change in the current situation of $21,853,093, and, moreover, since the plan was formulated, the Junction Bonds have been paid and equipment obligations have been reduced from $5,758,000, the amount provided for in the plan, to $4,540,000, a reduction in that requirement of $1,218,000.

Approximately $43,000,000 of the income available, but not used, for the payment of interest has been expended in permanent improvements and betterments. While the investment value of the debtor's property thus was substantially increased, the Commission's valuation, based on estimated future earnings, was not increased proportionately. As a result, the claim of the senior security holders has increased and the participation of the general mortgage bondholders has been pressed downward until it is now fixed at 10 per cent of the new common stock. Many of the improvements and betterments referred to above have substantially increased the capacity of the railroad to handle increased traffic as it arises. Central train control installed in many segments, where the greatest density of traffic obtains, gives to those segments, in a large degree, the equivalent of a double-track railroad and increases the number of trains that can be operated over the road and the volume of traffic that can be handled by the road. Other of such improvements have contributed to efficiency and economy in operations. These improvements have enabled the debtor to handle the great increase in traffic resulting from the war effort and have placed the debtor in a position to more economically and

efficiently handle a volume of traffic largely in excess of its prewar traffic, should future economic conditions produce such traffic. Under the plan approved and confirmed by the district court, 90 per cent of the common stock goes to the holders of the senior securities and 10 per cent to the general mortgage bondholders. As a result, should there be a substantial increase in the debtor's postwar traffic over its prewar traffic, 90 per cent of the increased earnings will inure to the benefit of the holders of the senior securities and only 10 per cent to the general mortgage bondholders, whose claim was decreased 90 per cent by reason of the failure to discharge interest accruals with income available therefor and the diversion of such income to the cost of such permanent improvements. It seems to me, under all these circumstances, that, in addition to the other adjustments required to make the plan fair and equitable, the Commission should endeavor to modify the plan so as to give relief from the situation that lets the full impact of the improvement program fall upon the claim of the general mortgage bondholders and accords them no corresponding benefits." 150 F. 2d 28, 40, 41–43.

From the confusing financial details one stark fact emerges. In 1939 the Commission found that the debtor would be able to earn enough in the future to provide an income on one-third of the General Mortgage bonds. 233 I. C. C. 515, 592. In the reorganization plan in 1943 the Commission concluded that the debtor would not earn enough to provide income on more than one-tenth of the General Mortgage claims. 254 I. C. C. 349, 359, 380. The capitalization proposed by the Commission in 1943 eliminated as valueless more of the total claim of the General Mortgage bonds and more of the face amount of these bonds than did the capitalization proposed by the Commission in 1939. Since 1939 the debtor achieved a position permitting it to make large debt reductions and

to reduce considerably its interest charges. It accumulated a very large net income in excess of its interest service, it expended large sums to decrease operating costs and improve its business prospects, so that the future earning power of the railroad was greatly increased. In the face of all these factors the senior security holders were given not only securities for the full amount of their claim but also all cash accumulations available for the reduction of the road's indebtedness. Improvements in the financial and physical structure of the road patently calculated to increase the profits of the future owners of this road have been made the basis of substantially wiping out one class of the present owners. Inequitable consequences such as these led the Circuit Court of Appeals to conclude that the plan failed to satisfy the command of Congress that as a matter of judicial judgment a reorganization plan must be found "fair and equitable."

To defeat the plan it is not necessary, however, to find it intrinsically wanting in fairness and equity. Congress did not authorize the enforcement of a plan for reorganization once it is found, as a matter of judicial judgment, to be "fair and equitable." Congress wrote into law another and a vital condition to the validity of a railroad reorganization plan. A plan must also commend itself as "fair and equitable" to the various classes of creditors. And if any class rejects it, the plan can prevail only if the District Court is warranted in finding that such rejection "is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts." 47 Stat. 911, 919 (1935), 11 U. S. C. § 205 (e).

Claimants who are thus entitled to vote on their interests as a class are surely not expected to vote as altruists any more than they are to be allowed to behave as unreasonable obstructionists. If that which Congress has written is not to be stricken out, we must recognize the referendum which Congress has lodged in each class of

creditors as a means of self-protection by each class of creditors and not as an occasion for empty dialectic. On a fair and practical construction of the power which Congress has seen fit to place in the hands of the various creditor classes, a class can be deemed not "reasonably justified" in exercising the right which Congress gave them to vote their interests, only if a court can say that no intelligent class of creditors, regardful of their class interests, but not obviously hostile to the common interest with which their class interest is involved, could have objected to the plan. Any other construction reads "reasonably justified" out of the statute. In effect that is what the district court has done. And this Court, with almost the candor of silence, appears to sanction such judicial deletion of what Congress has written. For it does not find that the General Bondholders were not reasonably justified from their intrinsic point of view to exercise their right to reject the plan. It does little more than assert this conclusion, apparently on the finding that the plan was in fact "fair and equitable." It imposes its judgment that the plan was "fair and equitable" upon the General Bondholders and thus in effect deprives them of the very right which Congress gave them to be judges of their own interests so long as the court cannot say they were capricious or greedy in their judgment. This Court seems to be of the view that if in its judgment a plan is "fair and equitable", it must appear equally fair and equitable to every class of creditors. Here, three circuit judges found the plan not "fair and equitable," yet this Court holds that the General Bondholders were not "reasonably justified" in not finding it "fair and equitable." This can only mean that the Court deems redundant, and therefore eliminates, the Congressional requirement that before a plan can be approved, it must commend itself to the judgment of a class of creditors exercising the kind of judgment that men are entitled to exercise in the pursuit of their

legitimate self-interest, as well as commend itself to the judicial sense of fairness.

In assuming that if a plan seems fair and equitable to a court, rejection of it by any class must be unreasonable, the Court not only disregards the contrary assumption on the basis of which Congress legislated. Such an attitude is also oblivious of the practicalities of the situation. To assume that if a court finds a plan is "fair and equitable" no class of creditors can be reasonably justified in rejecting it, is to assume that the ascertainment of fairness concerning so complicated a situation as a plan for a railroad's reorganization lies in the realm of even approximate certitude. Quite the opposite is true. A court in ascertaining whether a plan is fair and equitable is not engaged in ascertaining indisputable facts. It is forming a judgment, and largely a prophetic judgment, regarding a maze of factors, and as to each factor there is usually room for considerable difference of opinion. It is for this reason that Congress made it a condition for judicial approval of the plan that it appear fair and equitable in the voting system by the classes of creditors.

For an addition it was made by Congress to the recommendation of the legislation by Commissioner Joseph B. Eastman. As Federal Coordinator, he proposed to Congress that a court be authorized to confirm the reorganization plan despite the failure to obtain a majority vote of one or more of the affected classes of creditors, provided that the district court was satisfied in two respects: (1) that the plan "makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it"; and (2) that the judge was satisfied that the plan is "fair and equitable" "even if not so approved" by a class of creditors. See Coordinator's Annual Report for 1934, pp. 101–102, 237, 238.

But Congress deemed it in the public interest to give greater protection to the various classes of creditors than

the Coordinator suggested. In several respects Congress limited the power of courts to disregard a class vote against a plan beyond the safeguards proposed by the Coordinator. For present purposes it is decisive to note that Congress added to the protection formulated by the Coordinator by requiring that a judge, after finding that a plan is "fair and equitable," must also be satisfied and find that "such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts." I cannot escape the conclusion that to hold, in the circumstances of this case, that the General Bondholders were not reasonably justified in rejecting the plan is to decide that this requirement, purposefully written into the law by Congress as an addition to the requirement that the judge must find the plan to be "fair and equitable", is but a meaningless repetition of that requirement.

The undesirability of further delay in taking this road out of the district court, where it has been for more than a decade, is bound to press upon any court. But it ought not lead to confirmation of a plan which fails to satisfy the explicit prerequisites for approval laid down by Congress, particularly so where the result is as drastic as the Circuit Court of Appeals and the expert Senate Committee on Interstate Commerce have made manifest. See S. Rep. 1170, 79th Cong., 2d Sess., pp. 17–18, 40, 42, 67–68, 72–73, 91–95, 105–109, 121–123.

Congress has not curtailed, nor shown any desire to restrict, the right of self-protection which it gave to railroad creditors by the Act of 1935 and to which the result of this case appears indifferent. On the contrary, Congress has since given decisive proof that it disapproved the construction which courts have heretofore given to § 77, resulting in undue harshness to junior interests and promoting concentration of railroad control. It has emphatically indicated that the rights of junior interests, reflecting public interests, should be more carefully safe-

guarded. Whether Congress has been wise or unwise in manifesting this view is not our business to decide. But it is the business of this Court to respect what I find to be a clear enunciation by Congress of the conditions which alone authorize courts to sanction a railroad reorganization.

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